

The Legal Liabilities of Construction Management

The term “construction manager” seems plain enough, but is in fact used to refer to two distinct positions in the construction industry – construction managers *at risk* and *agency* construction managers. Each role is unique, with divergent responsibilities, and each faces a different set of liabilities. Few of these are covered in typical General Liability policies. More are covered by Professional Liability policies, especially those tailored to the construction industry, but people whose work revolves around construction management should be aware of the variable range of exposures they could face.

CM-at-Risk

The construction manager at risk (CM-at-risk) functions as a quasi-general contractor. A CM-at-risk directly hires the subcontractors necessary to complete the project, and therefore, like a general contractor, is customarily liable for the subcontractors’ performance. CMs-at-risk are also generally liable to the project owner for cost-overruns, project schedule delays and the quality of construction.

However, unlike a general contractor, who is typically selected through a competitive bidding process based chiefly on pricing, a CM-at-risk is usually selected on the basis of qualifications and a more flexible pricing model. The pricing model might include the negotiation of a fee plus reimbursable expenses, a guaranteed maximum price or some alternate project pricing methods. In a CM-at-risk contract, the parties may also agree to share savings in the event that the final cost of construction is less than the guaranteed maximum price. As the project begins, the CM-at-risk will usually obtain competitive bids from trade and specialty subcontractors.

CMs-at-risk also differ from traditional general contractors in that they frequently become involved earlier in the construction process, providing project owners with consulting services that cover a wide variety of pre-construction issues.

Working with a CM-at-risk is appealing to project owners who:

- Prefer qualifications-based selection of their contractor
- Need professional assistance in project planning
- Want to take advantage of potential cost benefits of competitive bidding for various trade contracts

Agency CM

The agency CM acts as an owner’s agent in advancing a project. Providing services to the project owner under the terms of a fee agreement, the agency CM acts primarily as a professional consultant to the owner, assisting in developing the project budget,



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master schedule, general conditions of the contract for construction, contractor selection, project procurement, requests for information (RFI) and change order management. The agency CM may also advise the owner regarding such activities as the selection of design professionals and specialty contractors, and obtaining project approvals.

While the specific services that an agency CM is contracted to provide may differ by project or by owner, one constant is that an agency CM does not directly hire trade and specialty contractors and subcontractors. Consequently, there is no privity of contract between the agency CM and the various trade contractors; therefore, the agency CM is not at risk for contractual liability to them, nor to the owner for their performance.

Because the services provided by an agency CM are acknowledged by the courts to resemble those of a professional services provider, rather than a general contractor, the agency CM is generally held to a professional standard of care in the provision of their services to the project owner.

During the construction phase, the agency CM may perform a range of services which typically include:

1. Acting purely as an agent, while not performing any actual construction
2. Providing an on-site staff to administer construction, and conducting coordination and scheduling meetings with contractors
3. Monitoring schedule and budget compliance and updating the owner with respect to unforeseen cost overruns and time delays
4. Advising the owner on how to successfully get back on schedule or within budget despite unforeseen events
5. Ensuring compliance with quality standards
6. Providing change order management and coordination
7. Reviewing contractors' applications for payments

Working with an agency CM is appealing to project owners who seek management assistance but prefer to be directly involved in selecting and negotiating with subcontractors. Alternatively, an agency CM can be hired in addition to a general contractor.

Potential Legal Liability

The chart below compares the legal liabilities faced by the two types of construction managers.

	CM-at-Risk	Agency CM
Liability to the Owner	<p>Subject to the typical liabilities of a general contractor, including liability for cost overruns, schedule delays, workmanship and quality of construction, and the performance of contractors and subcontractors.</p> <p>The CM-at-risk may also be liable for a negligent act, error or omission or breach of the standard of care for select elements of the services they provide the project owner.</p>	<p>Agency CMs are typically insulated from CM-at-risk liabilities, unless specific responsibilities are assumed contractually.</p> <p>The agency CM may also be liable to the project owner for a negligent act, error or omission or breach of the standard of care.</p>
Liability to Third Parties	<p>Typically there will be privity of contract between the CM-at-risk and the trade and specialty contractors, and the CM is at risk for contractual liability to them. These liabilities will typically arise from:</p> <ul style="list-style-type: none"> • Improper project coordination or scheduling • Improper supervision • Improper inspections • Failure to provide site access • Deficient submittal processing • Improper change order review and processing 	<p>While there is typically no privity of contract between the agency CM and the trade and specialty contractors, the courts have held that the absence of privity does not act as a complete shield for the agency CM's liability to injured third parties. Agency CMs may be found responsible to contractors and others for economic loss resulting from delay and disruption under contractual third-party beneficiary liability and under tort liability.</p> <p>These liabilities are discussed below.</p>

Third-Party Beneficiary and Tort Liability of Agency CMs

Third-Party Beneficiary Liability

Given that an agency CM does not directly hire trade contractors and no CM/trade contractor contracts exist, the trade contractor does not have a direct contractual claim against the agency CM. It has been held under certain circumstances, however, that a trade contractor may enjoy third-party beneficiary status with respect to the owner/agency CM contract, as trade contractors may be intended third-party beneficiaries of an owner/CM contract. It has been found that all contractors on a project directly benefit from the fulfillment of each other's contract. If one contractor fails to perform, the others will likely be delayed in their performance. Each contractor has a direct stake in the performance of all other contracts. Therefore, courts have found that trade contractors are intended third-party beneficiaries of the owner-CM contract, and as such they can sue an agency CM for failure to perform.

Tort Liability

Historically, third parties seeking damages for pure economic loss in tort were effectively barred from recovery as a result of the economic loss rule. Under this rule, an agency CM whose act or failure to act causes pure economic losses for a trade contractor – with no claim of personal injury or property damage – has no tort exposure. An increasing number of jurisdictions have abandoned the economic loss doctrine, and determined that the absence of privity does not bar a negligence action by one construction professional against another for economic losses, where reliance by the plaintiff was reasonably foreseeable.

Professional Liability Underwriters' Perspective

Construction management services – whether at-risk or agency – are a source of concern to Professional Liability underwriters. They are at pains to separate Professional Liability exposures – related to negligence in the provision of professional services – from General Liability exposures related to construction means and methods.

A review of Contractor's Professional Liability policy forms from different markets shows that most do not make a specific distinction between agency and at-risk construction management but include them variably under the descriptions of professional contracting services. Most policies include language aimed at removing cover for faulty workmanship, job site safety and other construction means and methods-based hazards. Often, this language describes activities of a construction manager.

Risk Regardless

A construction manager – whether a CM-at-risk or an agency CM – is clearly subject to a range of potential legal liabilities. Although the roles and responsibilities of the agency CM are often contrasted with those of the CM-at-risk – and held to be less risky – the agency CM remains exposed to liability on multiple fronts.

Given the professional services exclusion found in most General Liability policy forms, it is imperative that construction professionals providing construction management, project management and other non-traditional professional services carefully assess the scope of their exposure *vis a vis* their service or employment contracts. They should also take a close look at the ability of the insurance policies they have bought – or could buy – to respond in the event of a claim for negligence, tort or third-party liability.

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