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Today's endorsements may spell tomorrow's disasters

BY ERIC GRASBERGER

With the current emphasis in the building industry on construction defects, the list of endorsements that modify construction insurance policies is growing, creating a potential disaster for unsuspecting owners, contractors and design professionals.

Endorsements, which often reduce coverage otherwise provided by standard form policies, are frequently overlooked because the certificate of insurance – a document provided to summarize coverage – does not list or describe the endorsements.

Key endorsements may be hiding in your insurance documents; here are some tips to help minimize their impact.

• Mold and EIFS endorsements: Due to heavy litigation over mold and EIFS, an exterior insulating and finishing system also known as synthetic stucco, recent endorsements exclude coverage for these items. Some endorsements exclude only mold, fungus and spore remediation costs, but others exclude coverage for water intrusion damage of any kind. EIFS endorsements may exclude only certain types of EIFS systems or may broadly exclude coverage for even traditional cement stucco.

• Roofing endorsements: Because roofs are often contributors to water leaks, mold and personal injuries, some general contractor policies now include endorsements limiting coverage for roof-related claims.

• Continuous or progressive damage endorsements: The ability to stack policies to cover a multiyear loss may no longer exist under a continuous or progressive damage endorsement. Under this endorsement, only the policy in effect at the beginning of the loss will provide coverage. For example, if water damage occurs over five years, only the first year's policy limits – typically $1 million – will be available instead of all five policies stacked together – which can total $5 million.

• Cross-suit exclusions: If you seek additional insured status or insure multiple entities under the same policy, you should avoid the cross-suit exclusion. This exclusion prevents coverage for claims between parties that are both insured under the same policy, arguably including additional insureds. By seeking additional insured status, or by wrapping all of your company's entities under one policy – a common practice – you can inadvertently preclude coverage for claims that would otherwise be insured. From the insurance company's perspective, one should not be able to sue oneself to obtain coverage. Although this makes sense in some cases, it certainly does not in others – in particular, in the case of additional insured arrangements.

• Residential construction exclusions: An increasingly common endorsement excludes coverage for apartments, condominiums, town houses or other residential developments. If any contractor or subcontractor with this exclusion is employed on a residential project, you have no insurance coverage for damage he or she causes. A variation of this endorsement excludes coverage only for condominiums or town houses. However, even under this more limited exclusion, the possible future conversion of apartments to condominiums requires careful consideration of endorsements on any project.

So, are there solutions?

Indeed, there are limited solutions to the endorsement problem. First, in some cases, the exclusion can be removed by simply asking that it be removed. More commonly, however, an insured can buy back the coverage excluded by the endorsement.

One should obviously avoid products or projects that are costly or impossible to insure. Consider shopping your project until you find a contractor or designer whose policy does not include troubling endorsements; in some cases, you can look beyond the first-tier contractor to see whether coverage exists at a lower tier, such as a roofing subcontractor with roofing coverage.

Drafting a contract or request for proposal that prohibits certain endorsements is helpful, but you should expect that contractors saddled with these endorsements may bid on the project anyway. Deletion of the endorsements should always be confirmed.

Regarding the progressive damage endorsement, consider increasing your limits for each policy year to offset the inability to stack policies.

Finally, investigate whether a performance bond would add another layer of protection at an affordable price.

Do not expect to avoid all troubling endorsements, but be aware of them. The historic practice of simply relying on a certificate of insurance is no longer adequate. The insurance policy and the list of endorsements should be reviewed to understand the risks, and you should account for them in the financing and due diligence process of every construction project.

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