

WILENTZ

—ATTORNEYS AT LAW—

WILENTZ, GOLDMAN & SPITZER, P.A.

Allocating Risks Associated With Construction Defect Litigation Through Contractual Indemnification And Additional Insured Requirements

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Condominium associations and homeowners are typically not shy when it comes to filing lawsuits against the developer of their properties when they perceive that the construction or design is defective or deficient. This is equally true for construction projects where the developer performed no work whatsoever but rather retained, relied upon and paid substantial amounts to licensed architects, engineers and contractors to design and build the project. It is thus essential that developers appropriately allocate the risks associated with the development of a residential project to those parties that actually performed the work by including certain provisions in their contracts.

One provision that developers should include in their contracts to receive protection is a properly drafted indemnification provision, which holds the contractor or design professional responsible for any losses suffered by the developer resulting from their faulty or defective work. The provision can further protect the developer from liability where the developer is partially at fault for the defects, such as where the developer is alleged to have improperly supervised the contractor's work. To receive this additional protection under New Jersey law, the contract must expressly and unequivocally state that the indemnification clause provides coverage to the developer even where the damage was caused in part by the developer's fault or negligence. Developers are encouraged to draft the indemnification provision with such explicit and clear language given the possibility that any final determination ultimately made by a jury, judge or arbitrator will split responsibility between the developer and contractor.

Another provision that developers should include in their contracts is a properly drafted additional insured provision, which requires the contractor (and any of its subcontractors) to name the developer as an additional insured on its commercial general liability policies. The inclusion of an additional insured clause provides another means of protection, which may be even more so important when contractors are financially unable to defend and indemnify a developer against claims under an indemnification provision. Developers should require their contractors to not only provide them with certificates of liability insurance evidencing their contractors' coverage and the additional insured coverage, but also copies of the insurance policies, or at least the additional insured endorsements thereto, because the certificates do not afford additional insureds any rights under New Jersey law. Depending on the nature of the project, developers should also consider whether to require their contractors to obtain insurance without certain potentially applicable exceptions or exclusions to coverage such as exterior insulation finish system (EIFS) exclusions or residential condominium exclusions.

Developers should ensure that these provisions are included and correctly drafted in their contracts so that they have measures to protect themselves in the event that litigation arises. It is equally important that developers trigger those provisions by expressly demanding a defense and indemnity from their contractors and their contractors' insurers as soon as possible once litigation has been filed, or even threatened, to maximize the benefits these provisions can provide.

Have questions? Contact Don Taylor at 732.855.6434 or Dan Kluska at 732.855.6033.

REFERENCES:

Azurak v. Corporate Prop. Investors, 175 N.J. 110 (2003); Mantilla v. NC Mall Assocs., 167 N.J. 262 (2001); & Ramos v. Browning Ferris Indus. of S. Jersey, Inc., 103 N.J. 144 (1986) – decisions where New Jersey Supreme Court adopted and reiterated a “bright line” rule requiring explicit language in the contract that the indemnification and defense included the indemnitee’s own negligence for the indemnitee’s own negligence to be covered

Selective Ins. Co. v. Hopsicomm, Inc., 2014 WL 4722776 (N.J. Sup. Ct. App. Div. Sept. 24, 2014) & Porowski v. Rehm, 2008 WL 5273806 (N.J. Sup. Ct. App. Div. Dec. 22, 2008) – decisions where Appellate Division held that certificates of liability insurance do not provide any rights to the certificate holder and do not amend, extend or alter the coverage provided under the insurance policy based on typical and enforceable disclaimers in certificates stating that such certificates are issued as a matter of information only and confer no rights upon the policy holder

Attorneys

- Daniel J. Kluska
- Donald E. Taylor

Practice

- Construction Law