

RISK MANAGEMENT RECOMMENDATIONS FOR CONDOMINIUM PROJECTS

1. Avoid Inexperienced and Risky Developers. Condominiums are an easy market to enter because there are more builders and developers with experience in residential than any other building type. Condominium construction is considered “short jump” for developer/builders of single family or duplexes, but they may lack the experience and skills to manage a multi-unit housing project. These developers may be undercapitalized, unfamiliar in the risks of high-end, multi-family housing and, in particular, claims associated with condominium projects. Due diligence and background checks are essential for this project type. Be prepared to walk away from a project that is the first such project for a start-up developer unless you have direct experience with this client and have done a proper check of his or her credentials, abilities and financial resources.

[Recommendation: Conduct more in-depth client selection for condominium projects. Interview the developer/client for prior experience; contact past contractors and architects who have worked with this developer. Go see prior projects. Check with your lawyer and conduct a court-house check for prior litigation history or bankruptcy. If a start-up limited liability company (LLC), get records from the Secretary of State on the ownership and history of the company. A simple internet search can turn up considerable information on company history in litigation and newspaper articles about the developer’s past projects. Companies like Dunn & Bradstreet provide financial risk evaluation of businesses for a fee. Use this information in evaluating whether to take the project or not. Some architects require a “secondary sign-off” for condominium projects by an executive officer, principal or risk manager before any project is accepted. See Appendix D, which is a sample form for evaluation of condominium projects].

2. Identify Potential Problem Areas. Water intrusion is reported to be the number one defect in construction defect cases. Homeowners do not notice many other less obvious defects, but will usually notice stains on their walls or the water leaks at windows. Window leaks and roof leaks as well as cracked slabs, soil movement, drainage problems, cracks in walls, defective plumbing, cracked stucco and EIFS, structural

deficiencies, and improperly installed mechanical and electrical equipment are also frequent sources of condominium suits.

[Recommendation: Do an internal “peer review” or hire an outside “peer review” firm to review details and specifications in these areas before releasing the Contract Documents for construction. Promote early involvement, when possible, of the contractor in developing design details with input from specialty subcontractors. Discuss alternatives to EIFS and other materials that are the frequent source of construction defect claims. See other EIFS recommendations, below].

3. Maintain Quality. Some condominium developers are “over-leveraged” and, as a result, may give quality less consideration and more emphasis on cost-savings. When approached to “value engineer” the architect’s design, keep in mind long-term maintenance and quality materials. When quality is sacrificed in the short-term to get within a fixed budget, there are long-term costs when the building does not perform. This can lead to claims by unit owners when building systems do not perform to reasonable expectations.

[Recommendation: Require disclosure of developer’s financing; obtain outside financial review by your accountant, banker, or other financial advisor; Require periodic update from the developer on its financial position and financing. Include a contract clause like the AIA A201 General Conditions that the Owner must disclose financing up front and periodically, upon request. Docket periodic requests for financial information and designate someone in the office to follow up. Develop a form letter for this request. See Appendix C to this White Paper].

4. Avoid Reduced Scope of Architect Services. There is a perception by some developers that the architect’s fees are an unnecessary cost burden, created by the building permit process (need for sealed plans). Architects and engineers are often asked to provide bare minimum services, and limited or no construction phase services. Engineering consultants are sometimes hired directly by the developer or their work is performed via “design-build” by trade subcontractors (e.g. MEP, fire sprinklers) who may or may not have insurance for design errors or omissions. The architect may be asked to review their designs and assume liability for the work of consultants not selected or coordinated by the architect. In this scenario, the architect has less fee, less services and less control but more risk. The architect and its consultants cannot help to correct a problem they do not see during construction and their insurance may not contribute to resolve claims if the architect’s role is reduced. It is in everyone’s best interest to keep the

design professionals and their insurers engaged for the duration of the project to produce a quality project.

[Recommendation: Carefully evaluate reduced scope of services offered by the developer, and watch for areas of design performed by a variety of entities not under the control of the architect. With the increased risk of condominium projects, more design control can actually reduce your risk. Avoid fragmented delivery of design services where trade subcontractors and others provide only partial designs with little or no input or control by the architect over the end product selection or design. Watch for contracts that push design responsibility onto the architect for designs performed by others, or which limit the architect's role during any phase of the project, especially the construction phase].

5. Risks of Design-Build Subcontractors. When the parties agree to allocate some design services to the general contractor, via design-build subcontracts, and eliminate that from the architect's scope and fee, special consideration must be given to the process. Some developers will hand pick the subs based on price only, then direct the contractor to use those subs and require the architect to check or coordinate their work. This design work is often done by the lowest bidding sub, or by designers who lack proper qualifications and insurance. This also can create problems in coordinating that portion of the work with the architect's own design when these consultants are not under contract to the architect.

[Recommendation: Carefully review the scope of work for any design-build or "performance" specs. To the extent design services are agreed to be allocated to trade subcontractors: (1) Insist on qualified, experienced subs who carry professional liability insurance, and who retain licensed and insured designers; (2) Require sealed plans, by duly licensed firms and professionals, with adequate insurance; (3) Allow for adequate time to coordinate their work with the Architect's work].

6. Risks of Multiple Owners After Closing. Once the project is completed, sold and occupied there will be multiple unit owners, who have no direct contract with the architect. The chances of dissatisfaction by the owners are multiplied accordingly when there is a problem in the building which impacts on all of their individual living units. Since the architect has no contract with these end-users, the only vehicle to obtain protection is in the Owner-Architect Agreement with the project developer. These contracts can, however, require certain clauses to flow through to the unit purchasers and even the HOA by incorporation into sales contracts and HOA By-Laws and project Declarations.

[Recommendation: Include specific clauses from the Owner-Architect Agreement into the Unit Purchase Agreements between the developer and the unit buyers. More controversial, perhaps – instead of disclaiming any third party beneficiary status (as is often recommended) – consider making all subsequent unit purchasers express third party beneficiaries of the Owner-Architect Agreement. While this gives them the right to sue for breach of contract, it also passes on to them all of the protections and limitations of the Owner. In states where a third party can sue directly for economic loss or property damage, this is not an increase in exposure for architects.¹ By writing this clause broadly, the purchasers take all the same terms that are negotiated with the original Owner-Developer].

7. Retirement Condominium Projects. Some industry observers point out that condominium buyers are often elderly, especially in warm-weather retirement communities, like Florida, California and Arizona. Elderly people are often down-sizing and are likely to be first-time condominium buyers, less accustomed to high-rise living (which have less privacy, more noise, etc.) and are often less sophisticated purchasers. They may be more sensitive to their surroundings, to climate, odors and noise. This can result in unanticipated claims.

[Recommendation: Choose projects carefully. All condominium projects are potentially occupied by elderly. Watch for projects that are specially intended for retirement communities, etc. and evaluate the potential for increased claims.] Retain an acoustics consultant for sound transmission through walls and floor/ceiling assemblies. Be familiar with all state, federal and local accessibility requirements that apply to multi-family housing projects. Consider adding an accessibility consultant or senior living consultant to the design team].

8. Maintenance Budgets. Some HOA's have inadequate budgets for maintenance, insufficient maintenance staff and a reluctance to increase association dues to cover needed annual maintenance. This results in problems (especially in building skin, roof or common areas) being left unattended until too late. Untrained maintenance staff may not know what to look for or how to fix defects properly. Problems that might have been caught with proper maintenance go unattended and result in costly repairs later on.

¹ However, be aware that the statute of limitations for breach of contract actions may be longer than for negligence claims. Also, insurance may not cover a breach of contract claim. Consult your attorney and insurance agent for advice.

[Recommendation: Require in the Owner-Architect Agreement that the HOA By-Laws include an adequate maintenance budget, increased by a cost of living index annually, with inspection of roofs and other areas every two years or more often. If the HOA does not have a full-time maintenance employee, require some outside contractor to perform routine maintenance on a regular basis. The HOA should enter into maintenance contracts for major systems (including elevators, stairs, roof, structure, waterproofing, HVAC and plumbing systems), and will fund the costs of such maintenance contracts as part of the HOA operating budget. Agree to do an annual walk-through inspection of the premises for the period of the Statute of Repose (6 to 10 years in most states). Include the cost of this inspection in the initial design fee paid up front by the developer or have it paid out of association dues annually. Assist the contractor and developer in preparing a “Maintenance Manual” for the Project. Failure to follow the manual would be a defense to any claim in some states by statute] .

9. Class Action Lawsuits. Condominium associations (“HOA”) can provide a ready vehicle for class action lawsuits and their boards are sometimes targeted by plaintiff-oriented lawyers who market their services to condominium boards and HOA’s. The internet is full of such advertisements, some subtle and others more direct. As a result, with limited budget resources, the HOA may be enticed to sign up with a contingent fee arrangement that gives the lawyers from 33% to 50% of any recovery, but does not cost the HOA anything to pursue. The HOA By-Laws and project Declarations can require that decisions to file suit in matters involving all unit owners or common elements be made only after proper meeting and by a large majority of the association members and unit owners.

[Recommendation: There is new Federal Legislation aimed at curbing class action litigation, the Class Action Fairness Act (sign into law on Feb. 18, 2005)². HOA By-Laws can offer some added protection against class action suits by requiring a majority of the members/owners of the HOA to vote in favor of such suit, only after good faith discussions with the Architect.³ Add provisions to the Owner-Architect Agreement that require the developer to draft By-Laws and declarations requiring a “super-

² The Act limits contingent and other attorney's fees in proposed class action settlements; requires Federal court approval of settlements; restricts cases Federal court can hear; addresses rules of practice and procedure in such cases.

³ This is required by statute in some states already. See, e.g., Georgia, Kansas and Missouri right-to-cure laws, **Appendix G**.

majority” vote of the HOA, and a larger-than-average quorum; this assures that a small fraction of the association or its Board cannot bind the other unit owners to a lawsuit. Indemnity from the developer from such suits is another possibility due to the higher-than-normal risk of such suits].

10. Disappearing Developers. Condominium developers are often limited liability companies (LLC’s) set up just for one project and are nowhere to be found after they sell off the units. Many developers have no long term interest in the project once the units are sold, while others retain a property management role. This is really addressed above in all the other topics such as client selection and relationship with unit owners. However, when the client initially approaches your firm using one name, but then submits a contract under *a different name* – make an intelligent inquiry. Client names that include the “project name” followed by “LLC” are a warning that this is a single-purpose LLC, which may be undercapitalized and have no intention of being in existence once the project is finished and the units sold off.

[Recommendation: Watch out for single-purpose LLC’s and LLP’s and work only with developers who retain an ownership interest or property management role in the project after completion. It is uncertain how long a developer will retain that interest, so this can be misleading. Financial lenders will often require some personal guarantee or security interest before they will loan money to an under capitalized LLC. Why should the architect have any less protection? Require a personal guarantee or guarantee from the “parent” company of the developer; or take a security interest in the property, if it is clear the developer’s LLC or LLP has insufficient assets. Require proof of adequate insurance, just as the Owner does of its Architect.]

11. “Condo Conversions”. Condominium projects sometimes start out as apartment complexes that are later converted over to condominiums and sold off. So the architect starts off one way, assuming the developer will retain an ownership role, where there is just one property owner; but ends up with higher risk when the project is converted to condominiums with multiple unit owners and questionable maintenance abilities.

[Recommendation: Include a contract clause that prevents conversion to condominiums or which indemnifies the architect if the project flips to condominiums at a later date. Remember, however, that “indemnity is only as good as the indemnitor”, and a developer who dissolves an LLC after project completion may not be able to provide indemnity. Consider

requiring a personal guarantee of the indemnity, just like the project Lender will require before it risks its money. See Recommendation No. 10, above].

12. Joint and Several Liability. In some states, “joint tort-feasors”, i.e. persons whose combined negligence causes damage, are held “jointly and severally” liable to the injured plaintiff. This means that each defendant is liable for 100% of the damages; so if an architect causes 10% of the damage, but the contractor has no insurance and the developer is dissolved and long gone, a condominium unit owner could recover 100% of the loss from the solvent architect. Some states have abolished joint and several liability, but not all. See **Appendix F** to this White Paper.

[Recommendation: Expand the General Indemnity clause to cover any joint and several liability; however, be aware that indemnity from an insolvent, uninsured developer is not worth much. Consider requesting a personal guarantee in states which still have joint and several liability. See Recommendation No. 10, above].

13. Indemnity Provisions. For very high risk, low fee projects, consider an indemnity clause that expressly includes protection from claims alleging the architect’s own negligence, if the claim comes from unit owners or the HOA, stopping only at claims that were caused “solely” (100%) by the architect. If the owner, contractor, building maintenance, etc. contributed to the problem, there is full indemnity. But if the architect was the sole cause, then no indemnity. A growing number of states prohibit clauses that require one person (e.g. the Owner) to indemnify another person (e.g. the Architect) for the architect’s own negligence, called “anti-indemnity” laws. So obtain proper legal advice on whether such a clause will be upheld under the law that governs the contract.

[Recommendation: Use an appropriate indemnity clause that protects the Architect, at a minimum, from claims caused by the Owner, unit owners, condo association or contractor. Replace any overly broad Owner-drafted clause with something limited to the Architect’s own negligence. At the far end, for very high risk, low fee projects, require a clause that indemnifies the Architect except in cases of the Architect’s “sole” negligence. Add a governing law provision that incorporates the law of a state that does not have an “anti-indemnity” statute, either the law of the project location or the law of the architect’s office or even the developer’s home state, if any of these will enforce such a clause. Obtain legal counsel on the selection of state law to govern the contract].

14. Warranty Monitoring and Service. Some developers retain a property manager who is the sole point of contact with the contractor and architect for warranty problems. Ask to be notified of warranty problems during the period of the contractor's warranty. Keep accurate logs of: (1) Unit number; (2) Complaint; (3) Date of Complaint; (4) Investigation; (5) Solution; and (6) Date of Remedy. This will provide good documentation of the contractor's responsiveness to problems and give the architect notice of any recurring problems in multiple units, which may suggest a systemic problem. There are some inexpensive consultants who can set up a web site for the unit owners to log in their warranty complaints, so that the contractor, architect and appropriate sub gets prompt notice. If there is no property manager, set up this type of reporting system with the condominium association to make it easy to report warranty problems to the contractor by each unit owner.

[Recommendation: Set up a documentation system to log in warranty complaints and responses. Investigate web-based products that make this tracking easier. Build good service relations with the condo association and unit owners (who will have to vote to sue under the condo By-Laws). Consider whether this monitoring service should be offered as a Basic Service and, if so, whether it should extend beyond the contractor's normal AIA one-year warranty period. Recommend that the Owner set up a "warranty fund" based on the savings under the GMP contract cap, to be used for warranty repairs for a period of time, invested in an interest-bearing account].⁴

15. Bonding of the Contractor. This is a case-by-case decision. Discuss with the developer the added benefit of a surety bond which, unlike a contractor's general liability policy, generally has no exclusion for residential projects for bondable contractors and will bond over any contract clauses or warranties. The standard performance bond includes a one-year warranty period. Consider the benefits of an extended bond obligation through a "maintenance bond" for up to 3 years after Substantial Completion (or longer if available), with an extended warranty from the contractor.

[Recommendation: Discuss the benefits of surety bond protection with the developer and the benefits of an extended warranty from the contractor that is covered by a maintenance bond or other extended bond coverage. Recommend only bondable, experienced contractors. If a surety will not

⁴ AIA's 1997 edition of the A111 Owner-Contractor Agreement with cost of work plus fee, with a Guaranteed Maximum Price (GMP) already says in paragraph 12.2.5 that certain warranty repairs are to be paid from the GMP savings. That is the place to include this revision. See Recommendation No. 38, below.

bond the contractor, this may indicate a level of inexperience or financial instability not suitable for condominium work].

16. Contractor Selection and Insurance. Select qualified general contractors and trade subcontractors who have experience in high-rise or multi-family housing projects. Require all contractors and subcontractors to show that they are insured for residential, mold and EIFS (if available), since generally only contractors with a “mold awareness” program can get this insurance endorsement from some carriers.

[Recommendation: More emphasis on qualification-based selection of general contractor and trade subs for condominium projects, especially for areas that draw claims: HVAC, building roof and skin (EIFS), windows. Find out if the general contractor can qualify for a residential endorsement on its CGL policy and at what cost. Require insurance to be carried at a minimum for 5 years after substantial completion. Alternatively, explore an OCIP or CCIP, per Recommendation No. 37, below. Limits on such policies are often up to \$10 million for CGL, which can be achieved through an umbrella policy on top of the contractor’s standard policy limits].

17. Roofing and Building Skin Inspector. Additional consultants should be retained directly by the developer on condominium projects to inspect and test the exterior building skin and roof. At a minimum, there should be a weekly inspection, plus a final inspection at Substantial Completion and twelve-month warranty inspection, plus a written report issued to the architect, owner and contractor. This consultant-inspector should be hired directly by the developer, just like the surveyor and geotechnical consultant.

[Recommendation: Include a contract clause that requires the Owner to retain and pay for this inspection. Recommend a qualified and insured consultant. Discuss the benefits to the Owner and the overall project of such inspections. Avoid running this service through the Architect’s contract, even as an Additional Service].

18. Buyer Inspection Requirement. Prior to the purchase of each condominium unit, have the developer/owner require each buyer to fully inspect the unit and related common areas, using the services of a qualified residential inspector; and to sign a “Certificate of Satisfaction” as to the condition of the unit and have the purchaser accept responsibility for repair of any defects noted.

[Recommendation: Include a contract clause with a draft Certificate of Satisfaction; release the Architect and Developer of liability for claims that

should have been detected via such an inspection. Consider expanding the Release to cover any newly discovered defects if not promptly notified of problems and given an opportunity to cure].

19. Investigate Proper Use of Exterior Insulation Finish Systems (EIFS).

Due to the number of lawsuits related to exterior insulation and finishing systems (EIFS), and to the lack of insurance coverage for contractors covering EIFS claims, architects must use good judgment in specifying a building enclosure system that is trustworthy. EIFS systems have been reported to have a high number of claims for water intrusion, mold and property damage to the point that many insurers have excluded coverage for contractors on EIFS-related claims. Any use of EIFS should require a peer review of the architectural details, qualified and insured applicators, and strict contractor guidelines for inspection, installation, maintenance and warranty. There is an organization known as the Exterior Design Institute that certifies EIFS inspectors⁵. If a project demands use of EIFS, then require the Owner pay for inspections by a Moisture Warranty Certified Inspector or equivalent professional.

[Recommendation: Include specific EIFS inspection by an outside consultant to the developer as a contract requirement. Identify a good EIFS consultant to assist in peer review of the Contract Documents before they are released for construction; require the developer to front this cost as a risk management tool to protect the Owner. Inquire if the contractor and the EIFS subcontractor have insurance for this building system].

20. Contract Time Limits on Claims. AIA's A201 General Conditions has a time limit on claims by the Owner against the Contractor, but there is no similar limitation in the Owner-Architect Agreement (B141 or B151) for claims against the Architect. Also, such clauses may not survive completion of the Project unless there is specific reference in the contract. There is no reason why the parties cannot agree to a time limit on claims, just as in A201, and to extend this provision beyond Project completion so that the Owner has to make prompt claims (e.g. within 21 days of first observance of a defect) or waive it. This can also be included in Purchase Agreements with unit owners as well.

[Recommendation: Amend the Owner-Architect Agreement to add a clause which places a time limits on claims by the Owner against the Architect, such as within 21 days of first observance of a defect; retain the 21-day

⁵ The Institute's web site is at www.exterior-design-inst.com. The AIA Trust does not endorse this organization, but merely provides this information to its members as an example of related organizations to consider.

notice provision after completion and even termination of the contract. If not timely made, the claim is waived. Require an identical provision to be added to the unit Purchase Agreements].

21. Limitation of Liability. Include an appropriate limitation of liability clause that reduces (not eliminates) the architect's liability to a fixed sum, whether that be the Architect's fee, the available insurance coverage or some agreed amount. Research indicates that most courts will enforce these if the contract spells out the intention of the parties with great particularity and shows the intent to release from liability beyond doubt by express agreement..

[Recommendation: Include a clause that limits the Architect's liability to the Architect's fee, or to available insurance coverage if possible, or to an agreed lump sum amount. Document that this clause was negotiated and discussed. Some architects and engineers give a "base price" to clients and then a "discounted price" for the limitation of liability; this may be a useful tool in fee negotiations with the developer who is looking for ways to reduce project costs. Check applicable state law on whether such clauses are enforceable or require special wording].

22. Mediation and Arbitration. Always include a mediation clause and arbitration clause. Under the Right-to-Cure laws, **Appendix G**, mediation is required in some states but only between a "Claimant" and the contractor or design professional. However, "Claimant" is often defined as either: 1) an owner of a residence; or, 2) a representative of a homeowner's association. This may not include the developer if the developer has not retained any units. As a result, the mediation provision in the statute may not apply to a direct action between the developer and architect. A contract provision should be included in the Owner-Architect Agreement if one is not present already. The AIA B141 and B151 already requires mediation and arbitration, so no new language is needed when those forms are used and not modified. It would be good to include a mediation and arbitration clause in the HOA By-Laws and in the Purchase Agreements as well, so as to clearly spell out the procedures, venue, etc. for mediation and arbitration. Keep in mind, all jurors are homeowners and may be biased.

[Recommendation: Require mediation and arbitration in the Owner-Architect Agreement, in all subcontracts with the Architect's subconsultants, and in the HOA By-Laws and individual Purchase Agreements. If arbitration is not agreed to, then include a waiver of the right to jury trial so that the case is decided by an experienced trial judge, rather than jurors who may be more emotional, less neutral on a residential

dispute. Check for any special contract notices required by state arbitration laws (e.g. Missouri R.S.Mo. § 435.460).

23. Owner's Insurance. Keep clauses that require the Owner/Developer to carry and maintain property insurance, general liability insurance and, where appropriate, builder's risk insurance. Have your insurance agent review **the Owner's** insurance requirements (not just the architect's) of the Owner-Architect Agreement before signing. Often there is no such requirement of the Owner that identifies specific coverage and policy limits. With single-purpose LLC's as Owner, insurance is even more important.

[Recommendation: Require the Owner to provide you with its insurance information as a condition of the contract and have it reviewed by your agent or internal risk managers; develop a standard set of insurance requirements for the Owner with limits appropriate to each project. The HOA and/or condo unit buyers should be required to obtain and maintain satisfactory property insurance on completed condo units and will provide waivers of subrogation to the developer, architect and contractor for any losses and damage covered by such property insurance. Require that the Owner maintain its liability insurance at a minimum for 5 years after project completion].

24. Document, Document, Document. With digital photography today, it is easy to photograph a project and store pictures indefinitely. Keep good field notes of every site visit and photograph as much as possible. Archive those photos for at least six (6) years after final completion, preferably twelve (12) years, since the statutes of limitations and repose run from 6 to 10 years in most states. Two added years gives you a comfort against frivolous suits brought later after the statutes have expired.

[Recommendation: Keep a digital camera in the field trailer and in the car; download photos daily; back up with CD's; train staff on benefits of what they photograph; retain project documents for at least 12 years after project completion, including photos. Document the "mock up" unit, recommended below, Recommendation No. 34f].

25. Contractual Certificate of Merit Process. Some states have enacted special legislation that requires a "certificate" from an expert in the field to confirm that a lawsuit has merit before it can be filed against a design professional. However, many states have no such laws. Therefore, the parties can create their own process by contract, modeled after the laws in other states. This requires the owner to hire an expert architect

⁶ See Recommendation No. 34, below.

to evaluate claims against the architect and to provide a “certificate” that the claim has merit before it is filed. Absent the certificate of another licensed architect as to the merit of the owner’s claim, no suit can be filed or – if filed without the certificate – it can be dismissed. This should prevent frivolous lawsuits.⁷

[Recommendation: Add a contract clause that requires the Owner to hire a neutral licensed architect as an expert to provide a sworn affidavit stating the basis for his or her opinion that there is merit to a lawsuit or arbitration demand. Without this affidavit, the suit or demand cannot be filed. Suits or demands filed without the certificate of merit must be dismissed].

26. Limit and Control Re-Use of Documents. Include and retain contract language that retains the ownership and copyrights in the designs and documents, including any Architectural Works and any “derivative works”. Do not agree to contracts that would permit use of condominium documents on multiple projects, nor future phases, nor use by others if the agreement is terminated. By controlling the use and alteration of the architect’s design, the architect can avoid being pulled into litigation and claims on future projects or phases where the design is used by others. Plaintiffs’ lawyers often sue any party whose name appears in the project records, even if this was not a project designed by the architect. Condominium projects are capable of being repeated if the design is marketable, so control reuse by contract.

[Recommendation: Retain AIA-type clauses in B151 and B141 that control use and re-use of copyrighted designs; consider registering the copyrights with the U.S. Copyright office, which is a fairly inexpensive process that can be done with or without a lawyer. Forms and instructions for registration are available over the Internet at www.copyright.gov].

27. Promotional Materials. Developers may create artificially high expectations of buyers through over-zealous marketing materials. The Uniform Condominium Act creates a warranty for any representations made by the developer to the purchasers as to the physical characteristics of the plans, specs or project – even if the words “warranty” or “guarantee” are not used. However, by statute, this warranty can be excluded or modified by agreement of the parties. Disclaim any warranties that are so created by the developer and screen marketing materials for “puffing” that might result in a warranty claim by unit purchases.

⁷ While certificate of merit statutes are often challenged on a Constitutional basis, a negotiated contract clause is less likely to be found invalid.

[Recommendation: Include a contract clause that gives the Architect the right to review all marketing materials; disclaim any warranties created by the Developer and require indemnity if the Architect is sued by a unit purchaser based on warranties made by the Developer].

28. Use of a Joint Expert. Texas law permits the parties to request the court or arbitrator to appoint a neutral expert to review and report on claims. *See Appendix G.* In states with no such law, it is possible to contractually require an expert, neutral, who is jointly selected and paid 50-50 by the architect and owner/condo association, with both parties agreeing to be bound by the outcome of that report as to cause and cost sharing. Since some states (like Nevada) allow the cost of an expert to be charged as damages, the architect may as well pick up part of the cost up front in return for having a hand in selecting the expert and assuring the report is unbiased and with full information. To really work, this would have to have the agreement of the architect's consultants too.

[Recommendation: Discuss this during contract negotiations and, perhaps, identify a "neutral" expert in the contract for dispute resolution. Or for claims that arise, approach the Owner with idea of a shared expert, with each side to fund cost and share in selection. If no appeal within 30 days of the expert's decision, it is binding (just like AIA clauses which have been upheld in many states for years); include a similar clause in subcontracts with consultants so that they are equally bound].

29. Attorney's Fees Clause. Include a contract clause that allows the prevailing party to recover its legal fees and expenses. This will make the developer and any HOA think twice before turning the case over to a law firm on a contingency, if the HOA members might end up paying the architect's legal fees through an assessment by the HOA. Also, pass this obligation onto the appropriate subconsultants of the Architect.

[Recommendation: Include a prevailing party attorney's fees clause in the Owner-Architect Contract and in Subcontracts; add this to the Bylaws or the Declaration as well so as to bind the HOA].⁸

30. Waiver of Subrogation. Require the owner, the HOA and the unit owners to waive all rights of subrogation against the architect and its consultants. This prevents an insurer paying to repair some property damage and then suing the architect to recoup the amount paid out. The Uniform Condominium Act requires the HOA to carry

⁸ NOTE: Some insurance policies will not cover a contract provision like this if the Architect would not otherwise be responsible for the Owner's attorney fees. Check with your insurance agent and lawyer and discuss the risk vs. benefit.

property insurance on the common elements and that such policy waive subrogation against any unit's owner; but there is no such required waiver in favor of the architect.

[Recommendation: Add a waiver of subrogation clause (if not already in Owner-Architect Contract); and require this be put into the Declaration, HOA By-Laws and the Purchase Agreements].

31. Obtain a Unit as Part of Fee. One architectural firm reportedly acquires a condominium unit as part of its fee, so that the firm has a presence on the HOA and has first-hand knowledge of any problems in the building. This, of course, is a business decision to be made by each firm but the rapid appreciation of condominium real estate might suggest that this is a good business decision in many ways for risk management and as an investment.

[Recommendation: Consider taking a unit as part of compensation; use the unit to test ideas, etc.; maybe this is the “mock up” unit. Retain the unit for at least 10 years and get a member of the architectural firm on the HOA board. Use inside information and good neighbor relations to minimize claims].

32. Retain Ownership Rights in Building Skin. Some developers choose to deed over to the HOA and its members only the units and common areas but retain ownership of the roof and building skin for a period of years (say until the statute of repose has run, e.g. 10 years). This is a very aggressive concept that permits the developer to maintain those critical elements of the building, most likely to result in claims, and eliminates the basis for a claim by unit owners for property they do not control.

[Recommendation: Discuss benefits with developer; offer to draft up documents to accomplish this for review by developer's lawyer. Agree that the developer will retain those rights for a set number of years and will permit annual inspection by the Architect and Contractor of building skin, plus early notice of any defects or problems].

33. Require Disclaimer of Statutory Warranties. The Uniform Condominium Act creates implied warranties of quality, which can be excluded or modified by agreement⁹. This disclaimer can be as simple as saying “as is”, or “with all faults”, per the statute, if the condominium is not for residential use (e.g. office condo). One wonders why every developer would not use this disclaimer. For residential use, a “general disclaimer” of implied warranties is not effective; the seller must specify the

⁹ See Recommendation No. 27, above.

defect of failure to comply in a disclaimer. Require that this be included in every Purchase Agreement, with specific identification whenever the developer waives full contract compliance by the contractor, or accepts some defective work for a trade-out credit. If so, this should be basis for a disclaimer to protect the contractor, architect and the developer where the statutes allow this.

[Recommendation: Discuss with Developer, if not already doing this. Add a clause that requires the Developer to indemnify the Architect if no disclaimer is made of known defects in the Purchase Agreement, which defects have been accepted by the Developer or are known and are not repaired].

34. Build and Test Mock Up Unit. Even some developers recognize that before you build 100+ high end housing units and stack them, it makes sense to build a mock up and test it for acoustics, water test, etc. Include the cost of this in the Contract Documents and explain the benefits of assuring quality control by a mock up unit. This could be the Sales Office, which gets the developer an early unit to show buyers, yet lets the contractor and architect use it for testing purposes too.

[Recommendation: Discuss with Owner the benefits of a mock up and pass the cost onto the Owner. Have unit tested for acoustics, water test the skin and windows. Check details before they are repeated on the other units].

35. Shorten the Statute of Limitations on Statutory Warranties. The Uniform Condominium Act allows the parties to reduce the statute of limitations on both express and implied warranties from 6 years to 2 years. *See Appendix E.* For residential units, this has to be evidenced by a separate instrument, executed by the purchaser. Every developer should want to do this.

[Recommendation: Make this a contract requirement that a separate instrument be included with the unit purchase documents, signed by the purchasers].

36. Avoid High Risk States. Avoid condominium projects in high risk states, such as Arizona, California, Colorado, Nevada, North and South Carolina, Texas, Louisiana, Oregon, Washington and Florida. If your firm is located in these states, have regular in-house training on risk management. Use this White Paper as a discussion tool.

37. Use a CCIP or OCIP Insurance Program. Since many insurers exclude residential claims from the CGL policies carried by contractors and their subcontractors, it is in the developer's best interest to obtain a Controlled Insurance Program for the entire team that includes residential insurance coverage. This removes the question over

who is insured and who is not. The developer should pay for this insurance since it benefits the developer most in the long run. This is thought by some to be one of the most important risk management ideas for large condo projects since if the developer is a single-purpose LLC or other entity and the contractors and subs have no insurance, the architect may be the only insured, existing entity involved in the project. Keeping the contractors and their insurers engaged in solving and insuring defects will help avoid the “last man standing” problem for architects who may be sued for construction deficiencies simply because they are the only insured, solvent entity to blame. Also, in those states with Joint and Several Liability, architects may be exposed to liability for damages caused by the contractor which are not collectable due to lack of insurance coverage. Require that liability policies be maintained for a minimum of 5 years after project completion.

38. Warranty Reserve in Contract. Require the developer to put a reserve amount (or contingency) in the construction contract for warranty work. This does not get paid out until the warranty work is required; if there is any money in the fund at the end of the warranty period, come up with a method to share it with the contractor, or let the developer have it all. Another option is to give the fund to the HOA. *See* Recommendation No. 52. This pays for correcting warranty items out of the project budget. AIA’s standard Owner-Contractor Agreement, A111 (1997 edition) already contain clauses like this. See, e.g. par. 12.2.5 of AIA Doc. No. A111 (1997 edition), which reads:

§ 12.2.5 If, subsequent to final payment and at the Owner's request, the Contractor incurs costs described in Article 7 and not excluded by Article 8 to correct defective or nonconforming Work, the Owner shall reimburse the Contractor such costs and the Contractor's Fee applicable thereto on the same basis as if such costs had been incurred prior to final payment, but not in excess of the Guaranteed Maximum Price. If the Contractor has participated in savings as provided in Section 5.2, the amount of such savings shall be recalculated and appropriate credit given to the Owner in determining the net amount to be paid by the Owner to the Contractor.

39. Waiver of Consequential Damages. This is a standard provision in the AIA contracts, but on condominium projects, this can be a substantial issue. Be sure to include this if it is not already in the form contract being used. Do not let the developer strike this clause. Some firms will not sign any contract without this clause in it, based on experience with large claims. On a condominium project, there can be substantial consequential damages claims by unit owners who have to move out, etc. during repairs. The standard AIA clause from the A201 General Conditions (1997 edition) is printed below. The word “Architect” can be substituted for “Contractor”.

§ 4.3.10 Claims for Consequential Damages. *The Contractor and Owner waive Claims against each other for consequential damages arising out of or relating to this Contract. This mutual waiver includes:*

.1 damages incurred by the Owner for rental expenses, for losses of use, income, profit, financing, business and reputation, and for loss of management or employee productivity or of the services of such persons; and

.2 damages incurred by the Contractor for principal office expenses including the compensation of personnel stationed there, for losses of financing, business and reputation, and for loss of profit except anticipated profit arising directly from the Work.

This mutual waiver is applicable, without limitation, to all consequential damages due to either party's termination in accordance with Article 14.

40. Escrow Deductible Amount. Given the high likelihood of a claim against the architect on a condominium project, some firms include the amount of their deductible into their fee negotiations. However, if there are no claims, this goes to the “bottom line” as increased profits to offset the potential risk.

[Recommendation: Contract with the developer to put the amount of your deductible into an interest-bearing escrow account for an agreed period of time. For example, use the applicable statute of limitations or statute of repose. If there is a claim by the HOA, the escrowed funds are available to satisfy the architect's deductible. If there are no claims after the agreed period of time, the escrowed sum goes back to the developer, with accrued interest; or is split with the architect as incentive to reduce claims].

41. Pollution Liability Insurance. While many insurers for Commercial General Liability policies have invoked exclusions for such things as mold and EIFS, a contractor may still have insurance coverage for some mold-related claims under a pollution liability insurance policy, thus filling a gap in coverage.

[Recommendation: Add pollution liability insurance to the list of required insurance coverage to be carried by the general contractor, with limits appropriate to the project size, climate and location].

42. Retain AIA Statute of Limitations Clauses. AIA's B141 Owner-Architect Agreement (Par. 1.3.7.3) puts time limitations on claims by stating when the “statute of limitations” begins to run. This is regularly struck by owners and often agreed

to be struck by architects. However, for condominium projects, architects should be more insistent upon keeping these time limitations in the contract or replacing it with something even stronger, which start the running of the statute of limitations at Substantial Completion.

[Recommendation: Either keep the AIA clause in tact, or delete AIA B141, Par. 1.3.7.3 (1997 edition) and replace it with a new clause that does not shorten the statute of limitations, but simply waives claims more than five (5) years after Substantial Completion. That should be upheld, since waivers are generally valid and enforceable].

43. Mold Clause. There are lots of different mold clauses floating around and they generally all do the same thing. Some require prompt notice, others try to totally disclaim any mold liability. One used in lease agreements that says essentially if the mold spores in the building are no more than in the air outside, there is no basis for damages. This takes into account that in many areas there is generally a high mold count in the air we breathe each day; the weathermen even give this data nightly for those with seasonal allergies. In any event, the topic must be included in any set of condominium contract clauses.

44. Project Insurance. Some commentators recommend project policies as a way to reduce risk. However, most insurers have dropped project policies for the opposite reason; i.e. that developers who pay for a project policy are “more likely” to make a claim in order to get a return on that investment and, therefore, project policies “increase” risk of claims. Insurers are not writing project policies for condominium projects due to high risk. Be aware that a project policy for an apartment project may become void if the project is converted to condominiums.

45. Developer as Contractor. Some commentators recommend against working with a developer who also acts as the contractor due to conflicts of interest. However, a developer who also has the warranty obligations *as the contractor* would be more likely to do quality work, since any class action or condo association lawsuit would name the contractor as well as the architect as a defendant. If the contractor has experience as a developer, this combination adds some protection to the team structure. However, steer clear if both the developer and contractor entities are single-purpose LLC’s with limited assets, set up just for one project and dissolved upon completion.

46. All Building Systems Designed by Architect’s Team. Architects should insist that all key “project systems” be designed by the team of consultants assembled by the architect. This would eliminate any design-build on critical building systems by trade subcontractors or design by other consultants to the owner, with unknown skills or

insurance coverage. To the extent design-build is used for less critical building systems (e.g. communications, landscaping or lighting), *see* Recommendation No. 5, above.

47. Approval and Bonding of Subcontractors. Retain standard AIA provisions that require Owner/Architect approval of subcontractors, e.g. AIA’s A201 Par. 5.2.1 (1997 edition). Look for subcontractors who have been in business and will likely be around for years to come. Question any unknown names and require statements of qualifications. Discuss with Owner and Contractor the added cost/benefit of bonding any specific trade subcontractors.

48. Additional Insureds. Include contract clauses that add the owner and architect as additional insureds under the contractor’s CGL and umbrella insurance policies, usually at no added cost to the contractor. Require a Certificate of Insurance that shows the additional insureds prior to the first application for payment being approved. Be aware that coverage may be limited only to defects caused by the insured-contractor, for which the Owner and Architect are sued – known as “vicarious” liability.

49. Access Rights. Once the developer sells off all the units, the architect may no longer have access to the entire building, especially the living units. This will limit the ability to investigate complaints or determine the cause of problems. Delays can turn small problems into large ones.

[Recommendation: Include an express right of access, such as an easement, in the condominium By-Laws and Declaration so that the Developer can give access to the Contractor and Architect to and through the individual units and common areas to investigate. Discuss the benefits of such access rights with the Developer early on, before the condominium legal documents are finalized].

50. Quality Building Design. It goes without saying that with this high-risk building type, architects need to be careful during the design process. The best risk management tool is still good design details and qualified staff:

[Recommendation: (a) avoid unusual wall sections or roofing details; stick with traditional, time-tested wall sections, flashing and roof details; concrete or steel vs. wood frame (less subject to mold); (b) retain an acoustic consultant to review the design details for sound transmission between units, both walls and floor/ceiling assemblies – including footfall and plumbing; (c) consider hiring a roofing consultant to review building details prior to finalizing drawings or issuing bid packages; (d) waterproofing consultant; may be same as roofing consultant, but if not –

consider a consultant to review details and specifications for building skin; (e) assign experienced staff to all aspects of the project].

51. Buy Back the Unit. Some developers include a provision in the Unit Purchase Agreement that gives the developer the option to buy back a defective unit at fair market value in lieu of being sued by the unit owner. This gives the developer the right to re-purchase the condo unit, investigate and repair the defects and either retain the unit or re-sell it, perhaps at a profit. While this may not be an option for the architect, who has no direct contract with the unit purchasers, this is a recommendation that the architect can make to the developer to avoid a lawsuit by taking back the unit.

[Recommendation: Suggest to the Developer a clause for the Unit Purchase Agreements that would require written notice to the Developer of any defect, with an opportunity to inspect the unit. The Developer should have the option to cure the defect, or to have the unit appraised and to buy back the unit from the unit owner at fair market value, prior to any lawsuit or arbitration demand being filed].

52. Reserve Fund for HOA's Use. Require the Developer to set aside a contingency fund, say 5% of construction cost. When the project is completed, turn this fund over to the HOA as a start of the Building Repair and Maintenance Fund. In return for this cash payment, the HOA and unit purchasers agree to release the Developer and Architect from liability for design or construction defects.

[Recommendation: A waiver or release is more likely to be upheld or legally binding when given in exchange for something of value, called "consideration". In return for this 5% seed money for the HOA's use and benefit, require in the Owner-Architect Agreement that the Owner/Developer set up this fund, set aside the reserve funds and include a full release of liability in the HOA Bylaws or Unit Purchase Agreements of the Developer and Architect.]