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Design Professional's Duty of Care to Third-Party Purchasers

By Ryan L. Belka, Esq.

THE WORLD IS GETTING SMALLER AND our fences may not be high enough. Traditionally, courts have invoked the concept of duty to limit the otherwise potentially infinite liability which would follow from every negligent act. Though duty may arise through statute, contract, the general character of an activity or the relationship between the parties, one can generally choose, and more importantly predict, to whom one owes a duty.

The Court of Appeals for the First District recently decided a case expanding a design professional's duty of care to include third-party purchasers under both common and statutory law. In *Beacon Residential Community Association v. Skidmore, Owings & Merrill LLP et al.,* (No. A134542) architectural and engineering firms were hired to provide design services for the owner of Beacon Residential Condos, a 595 condominium unit residential complex (the "Project"). Beacon Residential Condo Association ("BCRA") brought claims against the design professionals asserting that it had a duty of care to the BCRA and to future residents of the Project.

Initially, the trial court dismissed the BCRA's claims stating "liability could not be premised on negligent design, and that BCRA was required to show that the design professionals had 'control' in the construction process, assuming a role beyond that of providing design recommendations to the owner." As would have been expected prior to *Skidmore*, as long as the final decision rests with the owner, the design professionals would owe no duty to the future residents of the complex.

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Donovan Hatem LLP Wins Summary Judgment on Appeal to the Massachusetts Appeals Court

By Matthew F. Lenzi, Esq.

DONOVAN HATEM LLP RECENTLY WON A MOTION ON SUMMARY JUDGMENT from the Massachusetts Appeals Court on behalf of its client, an engineering firm ("Engineer"). On May 23, 2008 Massachusetts Housing Opportunities Corporation ("MHOC"), a property development corporation, filed suit against the Engineer and its consultant after a wastewater treatment plant for its development projects vastly exceeded projected costs.

On October 2, 2003, while MHOC was in the process of developing a condominium project in Sterling ("Project"), it entered into an agreement with the Engineer to design a septic system for the Project. The Engineer, in turn, hired its consultant to provide information about the sewage treatment equipment and permitting advice. The Engineer began work on the design, and in November of 2004, concluded the Project could be submitted to the Department of Environmental Protection ("DEP") inexpensively under the Title 5 alternative system for piloting program. In December 2004, MHOC also received a bid for $300,000 from a third-party contractor based on the Engineer's design.

Upon receipt of the Project application, DEP informed the Engineer it needed to instead file an application for a major groundwater discharge permit, which required a dramatically increased fee. Upon filing the new permit, DEP subsequently informed MHOC that the Engineer's design was "administratively deficient" in various respects. On April 1, 2005, DEP formally denied the permit application and the Engineer subsequently transformed its original septic system design into a wastewater treatment plant and resubmitted the application for expedited review and approval.

The Engineer's consultant submitted to MHOC a $288,612 "final bid" for the materials to construct the Project in May 2005, which did not include labor costs. In the same time frame, the third-party contractor withdrew its prior bid due to the design changes. DEP finally accepted the new application in June 2005, and construction commenced.

MHOC filed its lawsuit in the Massachusetts Superior Court alleging professional malpractice, negligent misrepresentation, fraud, breach of contract, and violation of M.G.L. c. 93A. The Engineer and its consultant subsequently moved for summary judgment arguing that the tort and breach of contract claims were time barred. In response, MHOC claimed it was not until June 2005 that it became aware of the full cost to build the wastewater treatment plant. The Court agreed with the defendants, concluding that a three-year statute of limitations applied to those claims, and that MHOC had notice of its alleged injuries more than three years prior to the filing date. The Court also found that the c. 93A claim was not justified as the record did not reveal that any misrepresentations or omissions were coercive or extortionate. MHOC appealed the decision to the Massachusetts Appeals Court.

Statute of Limitations

On February 21, 2013 the Appeals Court upheld the Superior Court's decision and ruled in favor of the Engineer and its consultant. The Court reasoned that MHOC knew or should have known that the Project costs were escalating well before June 2005. MHOC had an active role in the design and permitting process, which began in December 2004, and was in contact with DEP having received the April 1, 2005 permit denial letter. With receipt of the denial letter, MHOC should have known a more sophisticated design was required, and by the time it received the consultant's "final bid", MHOC should have known that $200,000 was no longer a realistic budget figure.

Contract Claim

On appeal, MHOC argued the Superior Court erred in treating the contract action as a tort action for purposes of the statute of limitations. However, the Appeals Court concluded that, on its face, the claim was for a breach of an express warranty, but the "gist of the action" was one of tort, not contract. The contract action relies on the same factual allegations set forth in its tort claims; principally, that the Engineer negligently failed to identify the proper system required for the Project and subsequently concealed its true costs. The Court went

on to say that the promise the Engineer gave to MHOC was essentially for a certain budget figure for the Project, which did not guarantee a heightened level of workmanship. In other words, the "specific result" that MHOC alleges was not related to the proper operation or function of the wastewater treatment plant, but rather the Engineer's alleged negligence.

Conclusion

In upholding the Superior Court's grant of summary judgment for the defendants, the Massachusetts Appeals Court provided a succinct summary of the application of the discovery rule to negligence claims and the application of a three-year statute of limitations to contract claims where the "gist of the action" is negligence. For a breach of contract claim to survive scrutiny under the Court's standard, the "specific result" promised must be of such importance that it would "impose a higher duty on the defendants than the implied promise that…would [require them to] exercise that standard of reasonable care required of members of their profession."

Florida Design Professionals Are Now Protected From Personal Liability

By Lauren P. Marini, Esq.

IN LIGHT OF THE RECENT PASSAGE OF SENATE BILL 286 IN APRIL 2013, in most circumstances, design professionals will now be shielded from personal liability for damages resulting from allegations of negligence occurring within the scope of their professional services.

Florida Statute Section 558.0035 defines a "Design Professional" as an architect, interior designer, landscape architect, engineer, surveyor, or geologist. To benefit from the limitations of personal liability contained in Florida Statute Section 558.0035, the design professional must satisfy the following conditions:

- The contract must be made between the business entity and the client or with another entity for the provision of professional services to the client;
- The contract must not name the individual or agent as a party to the contract;
- The contract must include a prominent statement in uppercase font at least 5 point sizes larger than the rest of the text, citing the statute and stating that the individual employee or agent may not be held liable;
- The business entity must maintain any professional liability insurance required under the contract; and
- Any damages claimed must be solely economic in nature and not relate to bodily injury or property not subject to the contract.

The new law will take effect on July 1, 2013 for prospective claims, but is not retroactive. Therefore, any claims asserted against individual design professionals prior to July 1, 2013 are not subject to the limitation.

In light of this significant, beneficial change, it is in every design professional's best interest to thoroughly familiarize itself with the new law, and ensure that it strictly complies with the statutory conditions precedent for ensuring that individual liability is avoided. Since the law only recently went into effect, it is unlikely that design professionals' current contract templates satisfy the new statutory criteria. Therefore, it would be advisable to review and, if necessary, modify those contract templates to ensure the ability to take advantage of this very favorable development.

Architect Shielded from Liability by the Completed and Accepted Doctrine

By Adam C. Benevides, Esq.

THE "COMPLETED AND ACCEPTED" DOCTRINE HAS BEEN IN EXISTENCE for over a century. It is a defense that precludes a contractor's liability for personal injuries sustained by third parties where the work has been completed and accepted by the owner, even though the injury was caused by the contractor's negligence in performing the work or the contractor's failure to properly carry out the contract. There are generally exceptions to the rule such as when the work is dangerously defective, inherently dangerous, or imminently dangerous, where the contractor conceals defects in the work from the owner or where the work constitutes a nuisance per se. See 74 ALR 5th 523.

Until recently, the completed and accepted doctrine had only been applied to injuries caused by the faulty workmanship of building contractors. In *Neiman v. Leo A. Daly Co*[1]., however, the California Court of Appeals held that the completed and accepted doctrine applied to plaintiff's claims against the architect who designed and observed the construction of a theatre where the plaintiff was injured.

Plaintiff sustained injuries after falling down a set of stairs at the main stage of the Santa Monica Community College Theatre. Neiman sued various individuals including the architect on the project. Specifically, she claimed that the architect, as the project supervisor, was negligent because it did not ensure that the building contractor complied with its architectural drawings. The Plaintiff claims that she fell on a flight of stairs that failed to contain contrast marking strips as required both by state law and the architect's drawings. She also alleged there was insufficient lighting in this area.

The architect filed a motion for summary judgment. It argued that, unlike when it prepares architectural drawings, it owed no duty to third persons like the Plaintiff when it merely supervises construction work in its capacity as an agent of the owner. The Plaintiff conceded that her alleged injuries were not caused by a defect in the plans, but alleged that the architect was negligent, nonetheless, because it did not inform the owner, during the construction phase, of the missing contrast marking strips. The architect also asserted the completed and accepted doctrine. Under California law the completed and accepted doctrine is available where the work has been completed, the owner has accepted the project and the defect in the work *is not latent or concealed*. The architect also alleged the missing contrast marking strips were apparent by reasonable inspection.

Here, the main stage had been completed and accepted more than a year before the Plaintiff's accident. Accordingly, the architect argued the owner's acceptance of the project containing the alleged overt defect is an intervening cause for which it could not be liable. The Superior Court granted the architect's motion and the Plaintiff appealed.

On appeal, the Plaintiff's primary argument was that the failure to install the contrast marking strips was not a patent defect. In support of her position, she noted that the architect, the owner, and a representative of the Division of the State Architect did not notice the stripes were missing during a walk through shortly before the project was completed. The California Court of Appeals disagreed. The court noted that, had they been installed, the contrast marking strips would have been readily apparent to someone walking down the stairs. Therefore, their absence is an obvious and apparent condition.

This case is important because it recognizes that design professionals who serve as construction managers often take on different responsibilities with respect to their separate roles in a particular project. As such, defenses

[1] Neiman v. Leo A. Daly, Company, 148 Cal. Rptr.3rd 818 (2012).

generally available to contractors may also be available to a design professional when the alleged negligence arises not from an error or omission in their specifications and plans but, instead, when it acts as an agent of the owner in a supervisory capacity. While contractual language may create different legal obligations between the owner or a contractor, in the absence of a contrary statute, an architect acting in such capacity may have available all common law defenses as against third parties.

It should be noted, however, that this case arises from a jurisdiction that still recognizes the completed and accepted doctrine. Most jurisdictions have veered away from the doctrine in favor of a more modern approach called the foreseeability doctrine. Unlike the completed and accepted doctrine, the foreseeability doctrine does not release contractors from liability after the work is completed and accepted if it was reasonably foreseeable that a third person would be injured by such work due to the contractor's negligence or the contractor's failure to disclose a dangerous condition known to the contractor. In these jurisdictions, it does not matter whether a defect was patent or obvious to the owner. If it creates a dangerous condition, the contractor, and perhaps a supervising design professional, could still be liable. Since most jurisdictions adopt the foreseeability approach, project managers should always carefully inspect the work and review and compare the architectural drawings with the finished product to avoid any unintended consequences such as the injuries alleged in this case.

The Supreme Court of Florida Limits Application of the Economic Loss Rule to Products of Liability Cases

By Peter C. Lenart, Esq.

IN MARCH OF 2013, THE SUPREME COURT OF FLORIDA DECIDED *Tiara Condominium Association v. Marsh and McLennan Companies, Inc.,* No SC10-122 (March 7, 2013) ***(not final until time expires to file rehearing motion, and if filed, determined)***. In issuing its ruling on this matter, the Court greatly narrowed the application of Economic Loss Rule ("ELR"), a defensive doctrine that had long been helpful to providers of professional services, such as architects, engineers, and land surveyors.

In simple terms, the ELR is a doctrine created by Courts nationwide which sets forth the criteria by which a tort action is barred if the only damages suffered are economic in nature. Courts have found economic losses to be less than expected economic gains which are generally more properly governed by contract rather than tort law.

Contract actions are intended to address breaches of any agreement between parties, whereas tort law imposes a reasonable care of duty in order to avoid injury to persons and property. The Supreme Court of Florida noted, significantly, in its opinion that the ELR has its origin in products liability actions. In its *Tiara* holding, the Court elected to return the application of the ELR to such products cases. The Court also specifically declined to permit a provider of professional services (an insurance broker) to limit its tort exposure through the application of the ELR.

The Court's holding continues the Florida trend of limiting the application of ELR. In fact, the Court explained in the *Tiara* decision that the ELR had been applied too broadly in past Court decisions, and that it was necessary to return the ELR doctrine to the scope of its origins.

The *Tiara* decision has eliminated the distinction between causes of action in contract and tort raised against providers of professional services in Florida. Florida Professionals must now defend against tort claims brought in conjunction with breach of contract actions in the absence of the shield long provided to them by the ELR.

This legal development may have risk management, insurance cost, and insurance coverage implications for Florida Professionals. In order to manage this new, increased risk, Florida Professionals should always have their Professional Services Agreements reviewed by a business law attorney. Similarly, Florida Professionals should review their liability insurance coverage with their broker on an annual basis to make certain that they are maintaining adequate coverage levels.

Design Professional's Duty of Care to Third-Party Purchasers *continued from page 1…*

Skidmore changes that long-held presumption. "It is now well settled that an architect or engineer may be sued for negligence in the preparation of plans and specifications either by his client or by third-persons." The Court's determination was not whether or not a duty is owed to the third-party purchasers but, rather, the scope of that duty.

The determination whether a specific defendant will be held liable to a third-person, not in privity, is a matter of policy that involves a balancing of factors. The factors listed by the *Skidmore* Court are (1) the extent to which the transaction was intended to affect the plaintiff, (2) foreseeability of harm to the plaintiff, (3) degree of certainty that the plaintiff suffered injury, (4) closeness of connections between the design professional's conduct and the injury suffered, (5) the moral blame attached to defendant's conduct, and (6) the policy of preventing future harm. In practice, courts have split the sixth policy factor into three sub-factors (a) the potential imposition of liability out of proportion to fault, (b) the possibility of private ordering of the risk, and (c) the effect on the design professional's third-party liability.

Perhaps most concerning is *Skidmore's* analysis of the first factor of the balancing test which uses the limitation of liability clause to show the design professionals' actual knowledge that the transaction was intended to affect the plaintiff. The design professionals' agreements included standard limitation of liability language clearly stating that there would be no third-party beneficiaries to the Agreement, the design professionals were solely responsible to the Owner, and no condominium associations or future purchasers may become third-party beneficiaries to the Agreement. *Skidmore* uses these standard contractual limitations to expand the design professionals' duty of care to include claims for the exact parties these limitation clauses intended to preclude, third-party purchasers.

Though some factors might change factually on a case to case basis, such as the degree of certainty that the plaintiff suffered injury [3] or the moral blame attached to the defendant's conduct [5], some factors will always favor the claimants. The Court uses the fact that design professionals are licensed and their conduct regulated to conclude that the claimed harm is always foreseeable. [2] Since all design professionals are licensed and regulated *ipso facto* the harm is always foreseeable. Similarly, the Court concluded that design professionals' training and experience uniquely qualifies them to make decisions that a builder will presumptively rely on. As a result, if a departure in the standard of care is alleged as part of the claim, a court will always connect the defendant's conduct to the injury suffered. [4]

The Court's analysis of the sixth policy factor, and its sub-factors, does show some acknowledgment that expanding the scope of third-party liability has potential for unlimited liability. *Skidmore* considers the policy implications that expanding the scope of a design professional's duty would have on the industry, including design professionals being held responsible for a disproportionate share of the loss, increased housing costs, and the risk that design professionals will cease to design residential projects. [c]

However, the Court's analysis of the sub-factor "private ordering of risk" is further cause for concern. [b] *Skidmore's* analysis likens private ordering of risk to negotiating power. Where a third-party has negotiating power, the court will not expand the scope of duty because that third-party could have negotiated favorable contractual terms. In theory, this makes sense.

Unfortunately, what the court fails to recognize is that third-party purchasers of design services do not contractually negotiate with design professionals to privately order risk. Only the direct contracting party negotiates the scope of liability with the design professional. By definition, under this Court's analysis, no third-party purchasers of design professional agreements privately order risk and, thus, this sub-factor will inevitably lean toward expanding the design professional's duty.

Perhaps the case law will develop to limit *Skidmore's* findings only to residential design projects. Nevertheless, *Skidmore's* analysis applies to all design projects, and it signals that design professionals should be aware of their potentially expanded liability.

The cost of doing business is increasing. Design professionals must continue to exercise great caution when engaging in new design projects. As each project commences, detailed attention to contractual arrangements, including the intended market consumer, should be discussed with counsel. As always, an ounce of prevention is worth a pound of cure.

About Donovan Hatem

Donovan Hatem LLP is a multi-practice law firm with offices in Boston, New York and New Jersey. We serve a diverse clientele of private companies, nonprofit organizations, government entities and individuals. Our clients rely on our experience and expertise for focused advice and counsel that can minimize risk exposure.

The Professional Practices Group at Donovan Hatem includes more than 40 attorneys who provide highly-specialized counsel to architects, engineers, and construction managers. Our experienced trial lawyers represent design professionals in jury and non-jury cases in the northeast and nationwide, and at mediations, arbitrations, and other dispute resolution forums. In addition to professional liability claims defense, Donovan Hatem's scope of construction law expertise encompasses risk management, contract review, and general business matters.

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