

Contract Guide Course for Design Professionals:

Part II

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Learning Objectives

- Learn about key contract clauses creating risks;
- Learn to negotiate contract clauses to allocate risk more appropriately;
- Study and learn contractual risk transfer issues from case studies

Incorporation by Reference

- Be sure to obtain and read the “prime agreement” that is incorporated.
- Determine that the incorporated t’s and c’s don’t create greater responsibility than the t’s and c’s in your subcontract.
- Example clause is AIA C401-2007, 1.1 that provides:
 - “A copy of the Architect’s agreement with the Owner, known as the Prime Agreement ... is attached as Exhibit A and is made a part of this Agreement”.
- As a subcontractor, DP should:
 - (1) amend the above clause by adding exceptions for specific, identified articles of subcontract, and
 - (2) revise the Prime Agreement clauses as they will apply to you in the event they are unacceptable.

Indemnification (problem 1)

- Uninsurable “contractual liability” when DP agrees to indemnify for anything other than damages caused by DP’s negligence.
- Indemnity provisions are being written so broadly as to apply to:
 - First party breach of contract claims;
 - All errors and omissions even if not negligent;
 - All damages so long as DP is a little bit responsible
- No professional coverage specifically for the terms of “indemnity” clauses. Only covered if liability would have existed at common law.
 - So revise indemnity clause accordingly

Indemnification (Example bad clause)

- Example of overbroad and uninsurable indemnity agreement:
 - *“DP shall indemnify and save harmless the Client, and its officers, directors, employees and agents, from and against all liability, loss, cost or expense (including attorney’s fees) by reason of liability imposed upon the Client, arising out of or related to DP’s services, whether caused by or contributed to by the Client or any other party indemnified herein, unless caused by the sole negligence of the Client”*

Indemnification – (problem - “In Whole or in Part”)

- Beware of a clause stating DP will indemnify client for all damages caused “in whole or in part” by DP.
 - That language means DP will indemnify for ALL the damages even though caused only in small part by DP.
 - Insurance will only cover the damages to the extent caused by DP.
 - Reword a “in whole or in part” clause.

Indemnification (problem of 1st party claims)

- Indemnity should only apply to damages arising out of third party claims against the client.
- Some courts are confusing indemnity and allowing clients to use the clause to recover breach of contract claims against the DP, and to include their attorneys fees as part of their recovery.
- See next slide for sample indemnity clause limited to third party claims.

Indemnification (solution for third party claims)

- Example of reasonable indemnity clause:
- **“Indemnification.** Notwithstanding any clause or provision in this Agreement or any other applicable Agreement to the contrary, Consultant’s only obligation with regard to indemnification shall be to indemnify and hold harmless (but not defend) the Client, its officers, directors, employees and agents from and against those damages and costs that Client is legally obligated to pay as a result of third party claims, including the death or bodily injury to any person or the destruction or damage to any property, to the extent caused by the negligent act, error or omission of the Consultant or anyone for whom the Consultant is legally responsible, subject to any limitations of liability contained in this Agreement.

Indemnification: EJCDC solution

- *”Indemnification by Engineer:* To the fullest extent permitted by law, Engineer shall indemnify and hold harmless Owner, and Owner’s officers, directors, members, partners, agents, Design Professionals, and employees from reasonable claims, costs, losses, and damages arising out of or relating to the Project, provided that any such claim, cost, loss, or damage is attributable to bodily injury, sickness, disease, or death, or to injury to or destruction of tangible property (other than the Work itself), including the loss of use resulting therefrom, but only to the extent caused by any negligent act or omission of Engineer or Engineer’s officers, directors, members, partners, agents, employees, or Design Professionals. This indemnification provision is subject to and limited by the provisions, if any, agreed to by Owner and Engineer in Exhibit I, “Limitations of Liability.” EJCDC E-500 (2008), §6.10.A.”

Indemnification – Be sure the word “negligence” modifies everything.

- Poor wording may shift risk to DP for damages not caused by its own negligence. E.g.,
 - *“DP shall indemnify the Client for all claims, damages and expenses arising out of acts, omissions, errors or negligence of the DP.”*
- Notice that “negligence” is in the wrong place and fails to modify “acts, omissions and errors.” Thus, the indemnity applies to everything.

Indemnification – Increasing the Standard of Care

- Indemnification clauses that are not limited to negligence conflict with the normal Standard of Care.
- DP might be held to a perfection standard by the indemnification provision so it is liable despite having met the standard of care, i.e., it was not negligent.
- So a bad indemnity clause can trump a good standard of care provision in the contract,

Indemnification (the Uninsurable Duty to Defend)

- DPs should not agree to defend their Clients. No common law duty requires a DP to defend its client against third party actions.
 - No insurance coverage for the defense costs that the consultant pays on behalf of its client. The “contractual liability exclusion” applies.
- A contractually agreed upon duty to defend is triggered as soon as the claim is made because it is a separate duty from the duty to indemnify.
 - At least that is how most courts will interpret it. For example – California.

CONTACT Information & DISCLAIMER

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