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# PROFESSIONAL LIABILITY UPDATE

A Loss Prevention Newsletter for the Design Profession

## SPECIAL EDITION

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MSP PL—Special Edition 07/2005: "Position Paper: 'Attorneys Fees' Clauses—Should They Be Avoided?"

July, 2005



### Position Paper:

# “Attorneys Fees” Clauses Should They Be Avoided?

By Jeffrey W. Cavnac, CPCU, RPLU

An “attorneys fees” clause, also known as a “prevailing party” clause, is a provision in a contract that requires the loser to pay the winner’s legal fees. In the absence of such a provision, each party must bear its own legal costs.

Historically, the insurance industry and the legal profession have recommended that attorneys fees clauses be included in a design professional’s contract. An attorneys fees clause makes the plaintiff think twice before bringing a meritless claim. In other words, faced with the fact that they might have to pay the defendant’s legal costs in the event that they do not prevail, many plaintiffs will reconsider a questionable claim.

A typical attorneys fees clause might read as follows:

*“In the event of any litigation arising from or related to this Agreement, or the services provided under this Agreement, the prevailing party shall be entitled to recover from the non-prevailing party all reasonable costs incurred including staff time, court costs, attorneys fees, and all other related expenses incurred in such litigation.”*

Recently there has been some discussion as to whether or not an attorneys fees clause is, in fact, in a design professional’s best interest. This arises out of the fact that if your contract has such a clause and a court finds you negligent as alleged, you would have to pay the other party’s legal expenses in addition to the damages you caused. The contractual assumption of the other party’s legal defense costs may not be covered by your professional liability policy.

As you probably know, professional liability insurance covers your legal liability arising out of your negligent acts, errors or omissions. It does not cover your contractual assumptions of liability.

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Because of this, some insurance companies currently recommend against including an attorneys fees clause in your contracts.

### Underwriter Viewpoints

We approached a number of underwriters from different insurance companies that write professional liability coverage to get their opinions on this matter. Of the seven who responded, three were in favor of the position.

One underwriter stated, *“The clause is there to discourage frivolous claims, and we encourage its usage. Although one can never generalize about the outcomes of specific situations until one knows the facts and sees the actual contract language, we can say that, for the most part, we will cover prevailing parties’ legal costs unless a unique circumstance prohibits it.”*

Another underwriter opined, *“This has always been the typical ‘double-edged sword,’ and we have encouraged its use in most instances. We are not aware of any instances in which it has been used against our insureds; however, there have been situations in which it has been used to our insured’s advantage.”*

Four underwriters were not in favor of the provision, mainly due to the fact that the contractual assumption of another’s legal fees would not be covered under their insurance policies. (The three that agreed with the provision felt that in most cases it would be covered.)

One of the four stated, *“While prevailing party clauses can be a deterrent, if the insured is in fact the loser, costs incurred by the plaintiff which the defendant is contractually obligated to reimburse would be excluded contractual liabilities and uninsured as such.”*

Another underwriter said that the insured would be *“assuming liability by contract that they would not otherwise have, and therefore no coverage would apply.”*

### Attorney Viewpoints

We also approached three different attorneys who specialize in defense of design professionals. While one attorney was opposed to the use of the provision, one was in favor of it, and the other was on the fence, but leaning toward the negative view.

The attorney in favor of the clause stated, *“I recommend [attorney clause] provisions to all of my clients, since without them you cannot afford to pursue fee claims, which you’ll want to do far more often than you’ll be sued. I believe it tends to discourage frivolous claims against design professionals.”*

The attorney opposed to the provision stated, *“The attorneys fees clause is a trap for design professionals; i.e., it encourages owners to sue, and it is uninsurable under the typical E&O [errors and omissions] policy. The ‘American Rule’ is that parties bear their own attorneys fees in litigation. Attorneys fees clauses in professional services contracts are not at all typical, and they tend to promote litigation when the proper thing for the parties to do is to work out their difficulties, whatever they may be, through informal discussion or mediation, i.e., methods where attorneys are not involved.”*

The third attorney stated, *“I draft a fair number of contracts for design professionals, and I always discuss the pros and cons of an attorneys fees clause. The clause will deter a plaintiff from filing a claim out of fear of an award of attorneys fees. Most claims, however, settle, and the settlement typically includes a waiver of fees and costs. It is rare to have a recovery for fees and costs. My experience has been that when we are negotiating settlements and attempt to raise the fee clause for leverage, there is typically very little impact from such a maneuver. Lately the trend is not to include a prevailing party clause. I think that would be my current position, if asked to prepare a contract.”*

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### What Is a Design Professional to Do?

One alternative is to use an attorneys fees clause in your billing and collection provisions only. It would therefore be limited to suits for fees. Such a clause might read as follows:

*“In the event legal action is necessary to enforce the payment terms of this Agreement, the Consultant shall be entitled to collect from the Client any judgment or settlement sums due plus reasonable attorneys fees, court costs, and other expenses incurred by the Consultant in connection therewith and, in addition, the reasonable value of the Consultant’s time and expenses spent in connection with such collection action, computed according to the Consultant’s prevailing fee schedule and expense policies.”*

On a larger scale, the question is whether or not to include such a provision for all liability. Those in favor of using attorneys fees clauses will tell you that, first and foremost, it causes prospective plaintiffs to carefully evaluate their cases to make certain there is merit.

Secondly, they will point out that since most claim settlements typically include a waiver of fees and costs, it is rare that the provision will actually come into play. Having the provision in your contract, however, can strengthen your bargaining position when negotiating a claim settlement.

Those opposed to including attorneys fees clauses do so mainly because the design professional’s obligation to reimburse a plaintiff’s defense costs could be uninsurable.


Unfortunately, there is no correct answer. If you do not have a strong conviction for the use of an attorneys fees clause, then we recommend against it. Alternatively, you might consider using such a clause in your billing and payment section only.

The inclusion or exclusion of such a clause should be discussed with your attorney.

Our staff would welcome the chance to answer any risk management or insurance questions that you might have.



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President

*This article is written from a risk management and insurance perspective and is meant to be used for informational purposes only. It is not the intent of this article to provide legal advice, or advice for any specific fact, situation or circumstance. Contact legal counsel for specific advice. *

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