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The "Obligation to Defend" Your Client... and Why You Should Avoid It at All Costs!

Implications of a recent California Supreme Court Decision

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Back in January of 2002 our ***Professional Liability Update*** newsletter focused on the contractual obligation to defend your client **(see link to newsletter)**. While this "assumption of risk" may be insurable under a general liability policy, it is clearly not insurable under most professional liability policy forms. A recent California Supreme Court decision underscores the importance of avoiding the obligation to defend in connection with express indemnification provisions.

The case in question is known as Crawford v. Weather Shield Manufacturing, Inc. Crawford, a developer, contracted with Weather Shield to provide windows on a project. In the contract between the two parties, Weather Shield was obligated to not only indemnify and hold Crawford harmless, but also to *"defend any suit or action brought against Crawford founded upon the claim of such damage…"*

Several years after the project was completed some homeowners filed suit against Crawford alleging, among other things, that the windows were defective. Crawford incurred legal fees to defend the claim and ultimately settled with the homeowners and the cross-defendant subcontractors except for Weather Shield (and one other party). Crawford then brought an indemnity action against Weather Shield attempting to recover what it paid for indemnity as well as its legal costs in the homeowner litigation.

The lower court ruled that even although Weather Shield was found ***not negligent***, the firm still had an obligation to pay Crawford's legal fees. The rationale was that the "obligation to defend" was a separate issue from the "obligation to indemnify." The decision was upheld by the California Supreme Court.

In a nutshell, even though Weather Shield was determined to be not at fault, it was still responsible for the indemnitee's (developer Crawford) legal fees in the homeowner litigation.

As mentioned above, while this may be covered under a commercial general liability policy, it is ***not*** covered under most professional liability policy forms. Whereas a general liability policy's contractual liability coverage allows the insured to assume the tort liability of a third party, the contractual liability coverage under most professional liability forms is not nearly as broad. Contractual coverage under most professional liability forms is limited to liability that the design professional would have had in the absence of the contract. In other words, a design professional can agree to hold harmless and indemnify a third party for the consequences of the design professional's negligence, but any thing that goes beyond that negligence (such as the obligation to defend the client) would ***not*** be covered.

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From a design professional's perspective this is critical, since any general liability policy issued to a design professional will virtually always contain a Professional Services Exclusion. Because of this, it is critical that design professionals avoid the "obligation to defend" their clients in contractual indemnity provisions. Many clients may insist that this provision remain in the contract, and if they do, the design professional has a difficult business decision to make.

So What Is a Design Professional to Do?

1. Whenever possible, avoid contractual indemnity provisions.
2. If you must agree to contractual indemnity, seek to make it reciprocal and if that is not an option make certain the contractual language expresses that your obligation to indemnify must be caused by your professional negligence
3. **Avoid accepting defense duties in an indemnity provision**
4. If you cannot have the "obligation to defend" deleted, then seek to tie it to a negligence standard. Consider the following example:

> *"Consultant agrees, to the fullest extent permitted by law, to defend, indemnify and hold Client harmless against damages, liabilities and costs caused by the negligent acts, errors or omissions of Consultant in the performance of professional services under this Agreement, but only to the extent that Consultant is responsible for such damages, liabilities and costs on a comparative basis of fault between the Consultant and the Client after adjudication in a Court of Competent Jurisdiction. Consultant shall not be obligated to defend or indemnify Client for the Client's own negligence or for the negligence of others."*

Conclusion

From a risk management perspective, the indemnification agreement is a critically important element in an architect or engineer's Professional Services Agreement. The Crawford case has illustrated the dangers in a poorly worded indemnity agreement.

The good news is that many of your clients will understand that it doesn't make sense for you to assume obligations that are not backed up by your insurance program, and will agree to the modifications outlined above. After all, if the shoe were on the other foot, would your client assume responsibility for another's defense costs when it didn't do anything wrong?

Some clients may not be as reasonable. In those situations where despite your best efforts (and the efforts of your risk manager/insurance broker and attorney) your client remains unyielding, you will have a difficult decision to make.

We welcome any questions you may have.