

Duty to Defend: What This Means to Design Professionals

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An indemnification agreement contractually transfers risk from one party to another. These provisions are common in the construction industry. Typically, in a design context, the upstream party (an owner or general contractor if it is a design/build project) seeks to transfer risk to the downstream party (the architect or engineer) by way of an “indemnification” provision. Indemnities take many different forms, but basically it requires the downstream party to hold harmless and indemnify the upstream party from liability arising out of the design professionals work. It is also common for the upstream party to require the design professional to defend them in the event of a law suit. Unfortunately, this contractual assumption of defense is not insurable by the Architect or Engineer’s Professional Liability policy.

This coverage gap is not well understood by upstream parties. A Contractor signing the same agreement will likely have coverage for the assumption of risk under the company’s General Liability policy. But General Liability (GL) and Professional Liability (PL) policies differ when it comes to contractual liability. A GL policy provides broad contractual liability coverage whereas a PL policy provides limited contractual liability. While the GL policy covers the named insured for liability of others they assume contractually, the PL policy only covers the design professional for the consequences of the design professional’s negligence. 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 anything that goes beyond the design professional’s negligence is

not covered. The obligation to provide an immediate defense for the client would not be covered.

Construction claims are complex and expensive to litigate. Requiring a Design Professional to provide an upstream party with a defense (which can potentially cost hundreds of thousands of dollars) even if they haven’t done anything wrong is unfair and places a huge, potentially firm busting obligation on the Design Professional.

Some Recent History

While the insurability of an indemnity agreement has been an issue faced by design professionals since day 1, the topic got front page headlines based on two fairly recent California Court decisions (it’s important to point out that indemnity laws vary by state and



this article is focused on California’s indemnity laws). Both these cases reiterated that the “duty to defend” was separate from the “duty to indemnify,” and that a downstream indemnitor could be responsible for paying the upstream indemnitee’s legal fees even if the downstream party was determined to have done nothing wrong!

The California Supreme Court decided what has become known as the **Crawford Case** in July of 2008. Crawford (plaintiff), a developer, contracted with Weather Shield to provide windows for 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 all 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 for the window issues in the homeowner litigation. The lower court ruled that Weather Shield was not negligent. Regardless, Weather Shield 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 California Supreme Court upheld the decision. In a nutshell, even though Weather Shield was not at fault, it was still held responsible for the upstream party’s legal costs.

But the Court went even further. They clarified how the duty to defend was to be interpreted under California Civil Code Section 2782. The court clarified that the duty to defend is inherent to the duty to indemnify. In other words, there does not have to be an “express” requirement for defense; rather, it is built in to the indemnity obligation. Rule 4 of Section 2782 states, *“the indemnitor is bound on request of the indemnitee to defend actions or proceedings brought against the indemnitee in respect to the matters embraced by the indemnity.”* In other words, if there is no express statement that the indemnitor is not providing a defense, then the duty to defend exists.

A similar case was reviewed by a California Appellate court in early 2010, UDC v CH2M Hill (the **CH2M Case**). This case was the first litigation to interpret a design professional’s duty to defend subsequent to the Crawford case. CH2M Hill was retained by

the developer (UDC) to provide engineering and planning services in connection with a residential development. CH2M Hill was contractually obligated to *“indemnify ... Developer ... from and against any and all claims...to the extent they arise out of or are in any way connected with any negligent act or omission by Consultant....”* Furthermore, *“Consultant agrees, at his own expense, and upon written request by Developer or Owner of the Subject Property, to defend any suit, action or demand brought against Developer or Owner on any claim or demand covered herein.”*



After construction was completed, the homeowners association sued the developer, UDC, for various construction defects. UDC cross-complained against numerous subcontractors, including the engineering firm CH2M Hill. Ultimately, UDC settled with all of the subcontractors except CH2M Hill. This case went to trial. The jury ruled unanimously that CH2M Hill was not negligent and had not breached its contract. Relying on the Crawford case, however, the court ruled that, despite the fact that CH2M Hill was not negligent, it was still liable for UDC’s defense costs. Under the court’s interpretation, the duty to defend began when the homeowners association made claims implicating CH2M Hill’s work. The UDC case, in essence, demonstrates that the Crawford case holding will be applied to virtually anyone who enters into an indemnification agreement that does not include an express statement that the downstream party will not provide a defense.

Attempts to Fix the Problem

Senate Bill 972 was signed into law by Governor Arnold Schwarzenegger on September 29, 2010. This bill was an effort by the American Council of Engineering Companies of California (ACEC California) and others to reverse the decisions in both the Crawford and CH2M Hill cases. As originally written, the bill tied the design professional's obligation to defend or reimburse legal fees to the design professional's proportionate negligence. Unfortunately, as is so often the case, the final bill is substantially different from the original bill. As signed, the new law makes it illegal to "... require a design professional to indemnify (including the duty and cost to defend) a public agency except for claims that arise out of, pertain to, or relate to the negligence, recklessness, or willful misconduct of the design professional." The phrases "arise out of," "pertain to," and "relate to" are vague. If an upstream party alleges that a design professional was negligent, is that enough to trigger an immediate duty to defend? It is unclear, and opinions vary. Ultimately these questions will be answered by the courts.

Senate Bill 885 represents the design community's most recent attempt (2016) to amend California's current indemnity laws as it pertains to design professionals. This well intentioned legislation, which was shepherded by ACEC California, was intended to expressly eliminate a design professional's "duty to defend." SB 885 passed through the Senate Judiciary Committee with a 6-0 vote and was approved on the Senate Floor 26-4. Unfortunately, the opposition (public and private owners, contractors and subcontractors, and construction unions) became much more aggressive and SB 885 did not have the votes to pass the Assembly Judiciary Committee. As a result, the decision was made to pull the bill from the Committee Agenda.

Where Does This Leave the Design Professional?

What is clear is that the immediate obligation to defend, whether it is express or implied, is uninsurable under professional liability policies written for design professionals. So what is a downstream indemnitor to do?

Risk Management Seminar Series



Sexual Harassment Prevention Training

Friday, September 9, 2016

7:30am Registration

8:00am - 10:00am Program

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Handbooks: The Do's and Don'ts of Creating a Handbook

Friday, October 14, 2016

7:30am Registration

8:00am - 10:00am Program

Reserve Early, Seating is Limited!

To register, click on the 'register now' button in the announcement email, or contact Bethany Mongold at mongold@cavignac.com or call 619-744-0540.

If possible, all problematic contract provisions need to be negotiated out of the agreement. In order of priority, you should seek the following:

1. Try to avoid contractual indemnity provisions.
2. If you must agree to contractual indemnity, seek to make it reciprocal.
3. If you must agree to a unilateral indemnity, make certain that it is tied to your negligence; also be sure that there is an express rejection of the obligation to defend. You might consider something like this:

Notwithstanding any clause or provision in this Agreement or any other applicable Agreement to the contrary, Consultant agrees to indemnify and hold harmless (but not defend) the Client, its officers, directors and employees from and against damages and costs that Client is legally obligated to pay, 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.

Consultant shall have liability for reasonable and necessary defense costs incurred by persons indemnified to the extent caused by Consultant's negligence herein and recoverable under applicable law on account of negligence.

4. If the "obligation to defend" cannot be 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.

Option 4, while better than an unqualified express obligation to defend, may not accomplish your objective. It is conceivable that a court may interpret this

clause to mean that a separate duty to defend exists in addition to the duty to indemnify, and that the Downstream Party is required to begin defending the client (upstream party) as soon as a claim is tendered by the client, even if no determination of negligence has been rendered.

Final Comments

The decision of whether or not to agree to an uninsurable indemnity is only one factor in a design professional's Go/No Go process. If the project being considered is within a firm's sweet spot, has a fair fee, is with a good client and an otherwise acceptable contract, the decision may be made to bite the bullet and agree to the indemnity. After all, most litigated matters are settled prior to a final judgment by a jury or judge and generally the legal fees are one of the issues worked out in the final settlement. Regardless "Duty to Defend" is a big issue for a design firm with a potentially large downside.

When negotiating with your clients, it is important that they understand that you are not trying to avoid your responsibility. If you make a mistake for which you are responsible (and probably insured for) you will pay for it. What you don't want to do, however, is be responsible for someone else's mistakes. All you are asking is that the clause be fair and insurable.

Many clients will have a "take it or leave it" attitude when it comes to amending their indemnity provisions. They will say, "This is legal, and it is what our attorneys recommend." Regardless, you should always make the effort to amend the contract so it is fair and insurable. Your client might say, "Everyone else signs it," (which, by the way, probably isn't true). Your response might be, "If we make a mistake, if our performance falls below the standard of care required by the law, we will pay for it. However, we try to avoid assuming responsibility for mistakes made by others for which we are not insured. We take risk seriously, both yours and ours."

Every contract is different, and any language employed in a professional services agreement should be scrutinized by your legal and risk management advisors in light of the specific situation. There are no "cookie cutter" solutions to this complex problem. ■

LIVE WELL



WORK WELL

Health and wellness tips for your work and life—
Cavnac & Associates

Green Tea—More Than Just A Drink?

Recent studies have found a link between EGCG, a compound found in green tea, and increased brain functionality in areas associated with working memory. Mara Dierssen, a Group Leader at the CRG-Center for Genomic Regulation in Spain, decided to look into this link to see if EGCG could reduce some of the cognitive symptoms of Down syndrome.

Dierssen found that individuals in the study who were given EGCG exhibited higher results in visual memory, the ability to control responses, and the ability to plan or make calculations. Although it is too early to make concrete conclusions, these initial results have prompted plans for further studies.

What's Next?

Additional research is being conducted to see if EGCG has any beneficial effects on treating diseases like dementia and Alzheimer's. EGCG and its effects are an emerging area of study, so you can expect to hear more on this topic in the future.

This article is intended for informational purposes only and is not intended to be exhaustive, nor should any discussion or opinions be construed as professional advice. Readers should contact a health professional for appropriate advice.

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Taking Responsibility for Your Retirement Fund

Relying on pension funds and Social Security is no longer sufficient when planning for retirement. To help, the IRS has published the following tips to help you take charge of saving for retirement:

- **Set a goal:** Even if you can only save a small amount, setting aside money each month will get you in the habit of saving.
- **Open an Individual Retirement Arrangement (IRA):** Most Americans can open and make tax-deferred contributions to an [IRA](#).
- **Learn about your employer's retirement plan:** If you're covered under your employer's retirement plan, be sure to ask for your copy of the summary plan description to learn about your rights under the plan.
- **Review your benefits statement:** Your plan administrator can provide you with a benefits statement, which details your total plan benefits and the amount vested.
- **Sign up for 401(k) contributions:** If your employer offers a 401(k), you can select how much money you want taken out of each paycheck to be put into this account.
- **Take your minimum distributions:** If you're 70 1/2 years old, you're generally required to receive a minimum amount from your qualified retirement plan or IRA.
- **Estimate your Social Security benefits:** Use the Social Security Administration's [calculator](#) to do so.
- **Learn about your spouse's retirement plan:** Many plans provide spousal benefits. Be sure to read the plan's details to see if you are eligible.

Source: IRS

SUMMER SQUASH, ITALIAN STYLE

- 2 Tbsp. vegetable oil
- 1 large summer squash, thinly sliced
- 1 Tbsp. water
- ½ Tbsp. sweet, fresh basil
- 6 Tbsp. Parmesan cheese or Romano cheese, grated
- Salt and pepper (optional, to taste)

PREPARATIONS

- Using a large, ovenproof frying pan, heat 1 tablespoon of oil on medium high.
- Arrange the squash in the pan, add the water and season lightly with salt, pepper and basil.
- Cover and cook over medium heat for five minutes, or until tender.
- Sprinkle with the cheese and drizzle with the remaining oil. Place under a preheated broiler and broil until the cheese melts and browns slightly.

Makes: 4 servings

Nutritional Information (per serving)

Total Calories	110
Total Fat	9 g
Protein	4 g
Carbohydrates	4 g
Dietary Fiber	1 g
Saturated Fat	2 g
Sodium	115 mg

Source: USDA



Pokémon Go: Advice for Parents

Since its debut, Pokémon Go has garnered worldwide attention. News sources have been consistently reporting on both good and bad stories involving this app. As a parent, you may find yourself concerned about the dangers of Pokémon Go. To help keep your child safe, do the following:

- Remind them to pay attention to where they are going.** This is especially important when they are crossing the road and exploring unfamiliar territories, especially in residential areas, where players can be mistaken as trespassers.
- Remind them to be aware of their surroundings and strangers.** Discuss “stranger danger” tips with your child and tips for recognizing and evading dangerous situations.
- Encourage the “buddy system.”** Suggesting that your child play Pokémon Go with friends will increase both their safety and social well-being.
- Ask them to check in with you.** Consider setting up a system where your child updates you with his or her whereabouts periodically.



9.5 MILLION

Pokémon Go players worldwide

Average amount of time spent playing Pokémon Go daily:

43.4 MINUTES

\$1.6 MILLION

per day spent on in-app purchases

22 PERCENT

of players are between the ages of 13 and 17

Spotlight On



Cavnac & Associates is proud to support local and non-profit civic organizations, including Kids Included Together.



Kids Included Together (KIT) specializes in providing best practices training for community-based organizations committed to including children with and without disabilities into their recreational, child development and youth development programs.

Utilizing a blended learning style with interactive eLearning components, KIT's services are provided to its 63 affiliate organizations representing

over 304 sites in San Diego County. Since its inception in 1997, Kids Included Together (KIT) has trained over 25,000 youth providers in the best practices of inclusion.

Over 15,000 children with disabilities have been co-enrolled with over 265,000 children without disabilities at KIT affiliate sites. 72% of KIT's organizational budget is allocated to program expenses.

*For more information about Kids Included Together
visit www.kitonline.org*