PROFESSIONAL LIABILITY UPDATE

A Loss Prevention Newsletter for the Design Profession

MSP AEE 11/00: "Indemnities — Again Part II"" November, 2000

Indemnities — Again

Part II

The following material is provided for informational purposes only. Before taking any action that could have legal or other important consequences, speak with a qualified professional who can provide guidance that considers your own unique circumstances.

Indemnification originated in the construction industry to hold owners harmless from problems arising during construction. Since the contractor has 100% control of the job site, it's only fair that the contractor should indemnify (i.e., hold harmless) the owner for any site-related problems that arise.

Over time, however, the fairness concept behind indemnification has been corrupted. Today, architects and consulting engineers are often required to assume a large portion of the owners' risk – even though they do not have control over those risks.

Worse yet, this significant increase in liability assumed through a contractual indemnity, which is typically uninsurable (see sidebar, page 2) spells double trouble.

Our previous issue examined the dangers of client-drafted indemnities, identified the three types of owner-drafted indemnities you are likely to confront (broad-form, intermediate-form, and limited-form) and demonstrated techniques to persuade an owner to abandon the use of onerous indemnities.

But what if a client is insistent upon including an indemnity in your contract? In this article, we'll examine alternative forms of indemnities that have limited drawbacks and discuss situations in which you may want to turn the tables and ask for an indemnity from the client.

An Indemnity You Can Live With

The limited-form indemnity discussed in Part I is definitely the least of the three evils examined previously. An even better alternative, however, is a mutual indemnity that calls upon each party to indemnify the other, but only for the direct result of each party's own negligent acts.

If a client presents you with its own indemnity language, counter with a mutual indemnity such as the following example from ***The Contract Guide*** pub-

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lished by DPIC Companies:

Indemnification

The Consultant agrees, to the fullest extent permitted by law, to indemnify and hold harmless the Client, its officers, directors and employees (collectively, Client) against all damages, liabilities or costs, including reasonable attorneys' fees and defense costs to the extent caused by the Consultants negligent performance of professional services under this Agreement and that of its subconsultants or anyone for whom the Consultant is legally liable.

The Client agrees, to the fullest extent permitted by law, to indemnity and hold harmless the Consultant, its officers, directors, employees and subconsultants (collectively, Consultant) against all damages, liabilities or costs, including reasonable attorneys' fees and defense costs, to the extent caused by the Client's negligent acts in connection with the Project and the acts of its contractors, subcontractors or consultants or anyone for whom the Client is legally liable.

Neither the Client nor the Consultant shall be obligated to indemnify the other party in any manner whatsoever for the other party's negligence.

As a decidedly less desirable alternative, you may consider giving an insistent client some type of unilateral indemnity that limits the indemnity to that which is insurable.

Tie the indemnity to your negligence and purge the clause of any client-generated onerous language. Include the concept of comparative negligence, which holds you liable for only the portion of the damages for which you are responsible (unless your state law has an even more protective provision).

Finally, see that the indemnity is limited to the services called for under the agreement. These concepts are reflected in the following suggested language from DPIC:

Indemnification

The Consultant agrees, to the fullest extent permitted by law, to indemnify and hold harmless the Client against damages, liabilities and costs arising from the negligent acts of the Consultant in the performance of professional services under this Agreement, to the extent that the Consultant is responsible for such damages, liabilities and costs on a comparative basis of fault and responsibility between the Consultant and the Client The Consultant shall not he obligated to indemnify the Client for the Client's own negligence.

An Insurability Clause

There is one final “end-run” alternative if an owner insists on its own one-sided indemnity Include elsewhere in the agreement an insurability clause that calls for the nullification of any contract wording that would impose an uninsurable risk. An example:

Insurability

Client and Consultant agree it is essential that the Consultant's applicable insurance coverages apply to the project involved, for protection of the Client, the Consultant and any appropriate third parties that may be involved. Accordingly, the Consultant shall have this Agreement reviewed for insurability. Any element of this Agreement that is not insurable or whose insurability is questionable shall be considered null and void and the Client and the Consultant shall work together in good faith to replace any such element with another of similar intent, whose insurability is not in question. Should the Client require any special cov-

Why Indemnities Leave You Uninsured

Professional liability insurance specifically excludes liability you assume by contract; i.e., liability that would not be yours were it not for the fact that you specifically agreed to accept it.

The insurers' position on this issue is understandable. The rates they charge are based on certain assumptions they make about known risks, given the types of services a design firm performs, types of clients, amount of fees earned and so forth.

If insurers were to cover any and all additional risks a design firm agrees to assume by contract, the liability exposure could be made one thousand times greater than normal simply by the stroke of a designer's pen. ✷

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erage, policy amendment, or rider in order to attain insurability or for any other purpose, the Client shall pay the additional cost, if any.

Given the above, an uninsurable indemnification would be null and void. The parties would then work together to find alternative wording, such as a mutual or limited-form indemnity.

When the Client Won't Budge

If the client refuses to accept any alteration of an onerous indemnification, you have a business decision to make. You can accept the clause and the risk, hoping that the client will not ever have to apply the indemnity.

Realize, however, that you are opening yourself up to an unlimited financial exposure that virtually no professional liability insurance policy will cover. This option should only be considered with a very low-risk project type that your firm is thoroughly familiar with and that has been a claim-free area of practice.

The foolproof approach, of course, is to decline the engagement. This is a decision that may lose you an otherwise attractive project, but it may be the prudent choice to ensure your long-term survivability.

Plus, your willingness to hold your ground and walk away may just earn you the client's respect and perhaps result in an eleventh hour change of heart in demanding an unfair and uninsurable contractual agreement.

When You Want an Indemnity from Your Client

As stated, the original concept of indemnity is based in fairness, and no consultant should be reluctant to indemnify an owner from the design firm's own negligence, errors or omissions.

Likewise, there are certain instances where a design firm should not accept work on a project unless the client is willing to indemnify the consultant from risks. Such instances may involve hazardous waste, asbestos, condominiums, renovations or the possible unauthorized reuse of your design documents.

Indeed, there are times when an indemnity from your client for third-party claims is the only prudent approach. Your firm did not create the hazards and your role is to help the client overcome them.

In high-risk projects, an indemnity from the owner should be a requirement for your services. Such a contractual clause might read:

The Client agrees, to the fullest extent permitted by law, to indemnify and hold harmless the Consultant, its officers, directors, employees and subconsultants (collectively, Consultant) against all damages, liabilities or costs including reasonable attorneys' fees and defense costs, arising out of or in any way connected with this Project or the performance by any of the parties above named of the services under this Agreement, excepting only those damages, liabilities or costs attributable to the negligent acts or negligent failure to act by the Consultant.

For additional protection on very risky projects, particularly those involving hazardous conditions that you can't control or properly insure, talk

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to your attorney about the viability of asking your client for a *waiver* – an agreement from the client not to sue you.

A waiver is one of the most difficult provisions to obtain and to enforce, and some states have strict statutes applying to waivers. Therefore, keep the waiver and indemnity separate so that if the waiver is ruled invalid the indemnity isn't thrown out with it. Here is a sample waiver:

In consideration of the substantial risks to the Consultant in rendering professional services in connection with this Project, the Client agrees to make no claim and hereby waives, to the fullest extent permitted by law, any claim or cause of action of any nature against the Consultant, his or her officers, directors, employees, agents or subconsultants, which may arise out of or in connection with this Project or the performance by any of the parties above named of the services under this Agreement.

Conclusion

Indemnities are complex and have enormous liability implications. Have your lawyer examine any indemnity language with respect to the laws of the governing jurisdiction to determine exactly what your rights and exposures may be. Work, too, with your professional liability insurance specialist to determine the insurability of any indemnities you intend to sign.

Note that most professional liability policies will cover a limited-form indemnification that does not expand a design firm's liability beyond what common law says it must be responsible for in any event. Nonetheless, whenever a firm is considering acceptance of an indemnification clause, it should have the clause reviewed by an experienced agent or attorney first.✹

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