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# PROFESSIONAL LIABILITY UPDATE

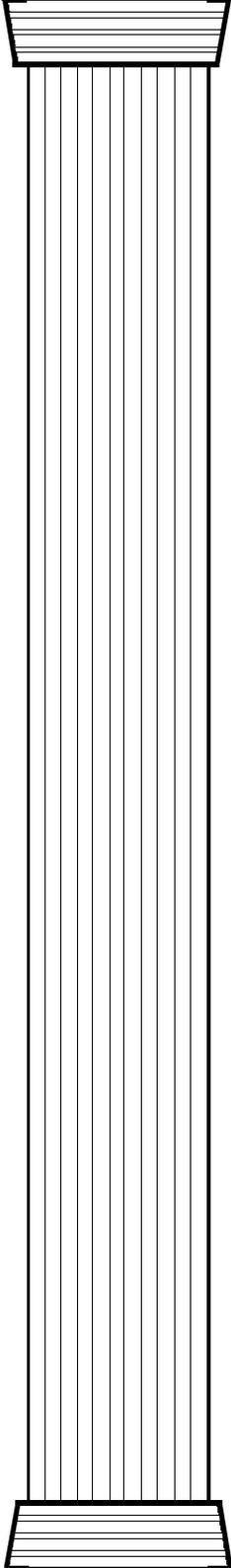
A Loss Prevention Newsletter for the Design Profession

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MSP AEE 05/01 "Understanding the Risks of Multiple-Prime Projects"

May, 2001

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## Contract Management: Taking the Bull By the Horns

All too often, design professionals are required to sign an onerous owner-generated prime agreement. Needless to say, these contracts are typically written to strongly favor the owner, and aspects of the contract may be not only unfair, but also uninsurable.

In a perfect world, the owner would sign the design professional's contract. This would be a well-written, equitable contract that would have certain built-in contractual protections that a design professional is entitled to.

Following is a list of provisions, which you might consider either including in your present master contact document, or adding to client-form contracts that you are asked to sign:

**1. Instruments of Service** - Design professionals should retain ownership of their documents, since the documents are instruments of professional service, and do not represent a product the design professional is selling.

### *Ownership of Instruments of Service I*

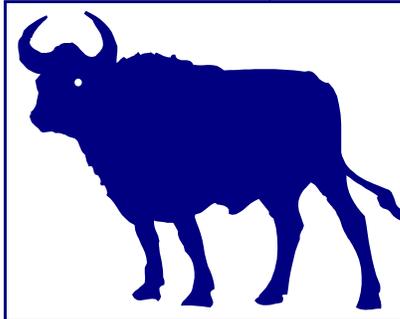
*All reports, plans, specifications, field data and notes and other documents, including all documents on electronic media, prepared by the Design Professional as instruments of service shall remain the property of the Design Professional.*

If this is not acceptable, at the least the client should agree to hold harmless and indemnify the design professional for the unauthorized reuse of the documents.

### *Ownership of Instruments of Service II*

*The Client acknowledges the Design Professional's construction documents as instruments of professional service. Nevertheless, the plans and specifications prepared under this Agreement shall become*

**Bull by the Horns**—continued on page 2



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**Bull by the Horns**—continued from page 1

the property of the Client upon completion of the work and payment in full of all monies due to the Design Professional. The Client shall not reuse or make any modification to the plans and specifications without the prior written authorization of the Design Professional. The Client agrees, to the fullest extent permitted by law, to indemnify and hold the Design Professional harmless from any claim, liability or cost (including reasonable attorneys' fees and defense costs) arising or allegedly arising out of any unauthorized reuse or modification of the construction documents by the Client or any person or entity that acquires or obtains the plans and specifications from or through the Client without the written authorization of the Design Professional.

**2. Standard of Care** – Many client form contracts will require you to perform to the “highest professional standards.” Although this is a good goal, design professionals should only have to perform in a manner consistent with that degree of care and skill ordinarily exercised by members of their profession practicing under similar circumstances.

#### ***Standard of Care***

*Services provided by the Design Professional under this Agreement will be performed in a manner consistent with that degree of care and skill ordinarily exercised by members of the same profession currently practicing under similar circumstances.*

**3. Defects in Service** – This provision requires the client to promptly report to the design professional any defects or suspected defects in the design professional’s services. The following clause would hold the client party responsible for any defect of which he or she was aware but did nothing to mitigate:

#### ***Defects in Service I***

*The Client shall promptly report to the Design Professional any defects or suspected defects in the Design Professional's work or services of which the Client becomes aware, so that the Design Professional may take measures to minimize the consequences of such a defect. The Client warrants that he or she will impose a similar notification requirement on all contractors in his or her Client/Contractor contract and shall require all subcontracts at any level to contain a like requirement. Failure by the Client, and the Client's contractors or subcontractors to notify the Design Professional, shall relieve the De-*

*sign Professional of the costs of remedying the defects above the sum such remedy would have cost had prompt notification been given.*

This alternative provision prohibits the withholding of any sum of money from payments due you unless you have been found legally liable for some alleged discrepancy of costs of changes in the work:

#### ***Defects in Service II***

*Payments to the Design Professional shall not be withheld, postponed or made contingent on the construction, completion or success of the project or upon receipt by the Client of off setting reimbursement or credit from other parties causing Additional Services or expenses. No withholdings, deductions or offsets shall be made from the Design Professional's compensation for any reason unless the Design Professional has been found to be legally liable for such amounts.*

#### **4. Opinions of Probable Construction Cost** –

Most design professionals are not professional cost estimators. In addition, they have no control over the cost of labor, materials and other elements, which make up the ultimate cost. As such, any construction cost estimate should be appropriately qualified.

#### ***Opinions of Probable Cost***

*In providing opinions of probable construction cost, the Client understands that the Design Professional has no control over costs or the price of labor, equipment or materials, or over the Contractor's method of pricing, and that the opinions of probable construction costs provided herein are to be made on the basis of the Design Professional's qualifications and experience. The Design Professional makes no warranty, expressed or implied, as to the accuracy of such opinions as compared to bid or actual costs.*

**5. Betterment** – A betterment provision spells out the fact that the design professional should not be responsible for paying the cost to add an item or component to the extent that that item or component would have been necessary anyway.

#### ***Betterment***

*If, due to the Design Professional's error, any required item or component of the project is omitted from the Design Professional's construction documents, the Design Professional shall not be responsible for paying the cost to add such item or component*

**Bull by the Horns**—continued on page 3)

to the extent that such item or component would have been otherwise necessary to the project or otherwise adds value or betterment to the project. In no event will the Design Professional be responsible for any cost or expense that provides betterment, upgrade or enhancement of the project.

**6. Risk Allocation** – Also known as “limitation of liability,” a risk allocation provision limits the design professional’s liability to a certain dollar amount. This reflects the fact that the design professional usually makes a very small profit on a given project (whereas the owner can make a very large profit), and as such, the design professional’s liability should not be unlimited.

#### ***Limitation of Liability***

*In recognition of the relative risks and benefits of the project to both the Client and the Design Professional, the risks have been allocated such that the Client agrees, to the fullest extent permitted by law, to limit the liability of the Design Professional and his or her subconsultants to the Client and to all construction contractors and subcontractors on the project for any and all claims, losses, costs, damages of any nature whatsoever or claims expenses from any cause or causes, so that the total aggregate liability of the Design Professional and his or her subconsultants to all those named shall not exceed \$\_\_\_\_\_, or the Design Professional's total fee for services rendered on this project, whichever is greater. Such claims and causes include, but are not limited to negligence, professional errors or omissions, strict liability, breach of contract or warranty.*

**7. Indemnification** – Indemnification is a contractual provision designed to allocate risk among the parties to the agreement. Ideally, a mutual indemnification is signed. Barring that, an insurable unilateral indemnification should be signed. Examples of both follow.

#### ***Indemnification I (Mutual)***

*The Design Professional agrees, to the fullest extent permitted by law, to indemnify and hold the Client harmless from any damage, liability or cost (including reasonable attorneys' fees and costs of defense) to the extent caused by the Design Professional's negligent acts, errors or omissions in the performance of professional services under this Agreement and those of his or her subconsultants or anyone for whom the Design Professional is legally liable.*

*The Client agrees, to the fullest extent permitted by law, to indemnify and hold the Design Professional harmless from any damage, liability or cost (including reasonable attorneys' fees and costs of defense) to the extent caused by the Client's negligent acts, errors or omissions and those of his or her contractors, subcontractors or consultants or anyone for whom the Client is legally liable, and arising from the project that is the subject of this Agreement.*

*The Design Professional is not obligated to indemnify the Client in any manner whatsoever for the Client's own negligence.*

#### ***Indemnification II (Unilateral, But Insurable)***

*The Design Professional agrees, to the fullest extent permitted by law, to indemnify and hold the Client harmless from damages and losses arising from the negligent acts, errors or omissions of the Design Professional in the performance of Professional services under this Agreement, to the extent that the Design Professional is responsible for such damages and losses on a comparative basis of fault and responsibility between the Design Professional and the Client. The Design Professional is not obligated to indemnify the Client for the Client's own negligence.*

**8. Information Provided By Client** – The design professional should be allowed to rely on the information provided by the client. In the event this information is incorrect, the design professional should not be held responsible.

#### ***Information Provided by Others***

*The Design Professional shall indicate to the Client the information needed for rendering of services hereunder. The Client shall provide to the Design Professional such information as is available to the Client and the Client's consultants and contractors, and the Design Professional shall be entitled to rely upon the accuracy and completeness thereof. The Client recognizes that it is impossible for the Design Professional to assure the accuracy, completeness and sufficiency of such information, either because it is impossible to verify, or because of errors or omissions which may have occurred in assembling the information the Client is providing. Accordingly, the Client agrees, to the fullest extent permitted by law, to indemnify and hold the Design Professional and the Design Professional's subconsultants harmless from any claim, liability or cost (including reasonable attorneys' fees and costs of defense) for injury or loss arising or allegedly arising from errors, omissions or*

inaccuracies in documents or other information provided by the Client to the Design Professional.

**9. Hidden Conditions** – A design professional simply cannot know everything about a given project, especially a remodel. In the event that hidden conditions increase the cost, time frame or any other aspect of the project, the design professional should not be held responsible.

#### ***Verification of Existing Conditions***

*Inasmuch as the remodeling and/or rehabilitation of an existing building requires that certain assumptions be made regarding existing conditions, and because some of these assumptions may not be verifiable without expending additional sums of money or destroying otherwise adequate or serviceable portions of the building, the Client agrees, to the fullest extent permitted by law, to indemnify and hold the Design Professional harmless from any claim, liability or cost (including reasonable attorneys' fees and costs of defense) for injury or economic loss arising or allegedly arising out of the professional services provided under this Agreement, excepting only those damages, liabilities or costs attributable to the sole negligence or willful misconduct of the Design Professional.*

**10. Job Site Safety** – Job site safety is the responsibility of the contractor. This provision spells that out, and makes it clear that the design professional has no responsibility for job site safety.

#### ***Jobsite Safety***

*Neither the professional activities of the Design Professional, nor the presence of the Design Professional or his or her employees and subconsultants at a construction site, shall relieve the General Contractor and any other entity of their obligations, duties and responsibilities including, but not limited to, construction means, methods, sequence, techniques or procedures necessary for performing, superintending or coordinating all portions of the Work of construction in accordance with the contract documents and any health or safety precautions required by any regulatory agencies. The Design Professional and his or her personnel have no authority to exercise any control over any construction contractor or other entity or their employees in connection with their work or any health or safety precautions. The Client agrees that the General Contractor is solely responsible for jobsite safety, and warrants that this intent shall be made evident in the Client's agreement with the General Contractor. The Client also agrees that the Cli-*

*ent, the Design Professional and the Design Professional's consultants shall be indemnified and shall be made additional insureds under the General Contractor's general liability insurance policy.*

**11. Delays** – Design professionals should be held responsible for delays caused by their negligence. Delays other than this should not be their responsibility. This provision will help protect you against claims by your client for delays caused by factors beyond your reasonable control:

#### ***Delays I***

*The Design Professional is not responsible for delays caused by factors beyond the Design Professional's reasonable control, including but not limited to delays because of strikes, lockouts, work slowdowns or stoppages, accidents, acts of God, failure of any governmental or other regulatory authority to act in a timely manner, failure of the Client to furnish timely information or approve or disapprove of the Design Professional's services or work product promptly, or delays caused by faulty performance by the Client or by contractors of any level. When such delays beyond the Design Professional's reasonable control occur, the Client agrees the Design Professional is not responsible for damages, nor shall the Design Professional be deemed to be in default of this agreement.*

The following clause addresses the potential costs caused by excessive and inappropriate RFI's:

#### ***Delays II***

*The Client warrants he or she will cause the Contractor to review any requests for information (RFIs) submitted by subcontractors prior to submission to the Design Professional to ensure such RFIs are not already clearly and unambiguously answered in the Contract Documents. The Design Professional shall be paid by the Contractor for his or her time in reviewing RFIs, which are already clearly answered or inferable from the Contract Documents in accordance with the Design Professional's standard rates. In the event of a disagreement over such compensation, the judgment of the Client's representative shall prevail.*

**12. Assignment** – Ideally, neither party can assign the agreement without the permission of the other.

#### ***Assignment***

*Neither party to this Agreement shall transfer, sublet or assign any rights under or interest in this*

Agreement (including, but not limited to, monies that are due or monies that may be due) without the prior written consent of the other party.

**13. Dispute Resolution – Mediation** should always be used as the first option when resolving disputes. If mediation is not acceptable, **arbitration** (or some variation) should be considered, but it should **not** be mandatory. (Mandatory binding arbitration is preferred on disputes up to a certain dollar amount. )Litigation, of course, is an alternative when all else fails.

#### **Mediation**

*In an effort to resolve any conflicts that arise during the design or construction of the project or following the completion of the project, the Client and the Design Professional agree that all disputes between them arising out of or relating to this Agreement shall be submitted to nonbinding mediation unless the parties mutually agree otherwise.*

*The Client and the Design Professional further agree to include a similar mediation provision in all agreements with independent contractors and consultants retained for the project and to require all independent contractors and consultants also to include a similar mediation provision in all agreements with subcontractors, subconsultants, suppliers or fabricators so retained, thereby providing for mediation as the primary method for dispute resolution between the parties to those agreements.*

#### **Arbitration**

*In the event the parties to this Agreement are unable to reach a settlement of any dispute arising out of the services under this Agreement, involving an amount of less than \$\_\_\_\_\_, in accordance with Paragraph \_\_\_\_\_(Dispute Resolution), then such disputes shall be settled by binding arbitration by an arbitrator to be mutually agreed upon by the parties, and shall proceed in accordance with the rules of {insert appropriate reference to a specific arbitration service's set of rules, such as the Construction Industry Arbitration Rules of the American Arbitration Association or the Center for Public Resources' Rules} then pertaining. If the parties cannot agree on a single arbitrator, then the arbitrator(s) shall be selected in accordance with the above-referenced rules.*

**14. Termination of Services –** Ideally, the agreement can be terminated by either party. This provision allows either you or the client to terminate the contract for any reason:

#### **Termination I**

*Either the Client or the Design Professional may terminate this Agreement at any time with or without cause upon giving the other party \_\_\_( \_\_\_\_ ) calendar days prior written notice. The Client shall within \_\_\_( \_\_\_\_ ) calendar days of termination pay the Design Professional for all services rendered and all costs incurred up to the date of termination, in accordance with the compensation provisions of this contract.*

The following provision gives you a more limited range for which you may terminate:

#### **Termination II**

*The Client may terminate this Agreement at any time with or without cause upon giving the Design Professional \_\_\_(\_\_\_\_)calendar days prior written notice. The Design Professional may terminate this Agreement upon giving the Client \_\_\_(\_\_\_\_) calendar days prior written notice for any of the following reasons:*

*[List of specific circumstances, such as:]*

- a. **Breach** by the Client of any material term of this Agreement, including but not limited to Payment Terms.
- b. **Transfer of ownership** of the project by the Client to any other persons or entities not a party to this Agreement without the prior written agreement of the Design Professional.
- c. **Material changes** in the conditions under which this Agreement was entered into, coupled with the failure of the parties hereto to reach accord on the fees and charges for any Additional Services required because of such changes.

The following provision, which requires the client to reimburse you for expenses associated with stopping the project, can be added to either of the preceding clauses:

#### **Termination III**

*The Client shall reimburse the Design Professional for all expenses reasonably incurred by the Design Professional in connection with termination of this Agreement, including but not limited to demobilization, reassignment of personnel, and space and equipment costs.*

**15. Third-Party Beneficiaries –** This provision precludes any third party from being considered a beneficiary to the contract. The contract should only run between the design professional and the client.

### **Third Party Beneficiaries**

*Nothing contained in this Agreement shall create a contractual relationship with or a cause of action in favor of a third party against either the Client or the Design Professional. The Design Professional's services under this Agreement are being performed solely for the Client's benefit, and no other entity shall have any claim against the Design Professional because of this Agreement or the performance or non-performance of services hereunder. The Client agrees to include a provision in all contracts with contractors and other entities involved in this project to carry out the intent of this paragraph.*

## **Conclusion**

Needless to say, this is not an all-inclusive list of every contractual provision you might consider putting in your master contract or inserting into a client contract form. Every contractual negotiation is different, as is every project and client. Regardless, it is a good idea to have a strategy when negotiating contracts as well as an attorney and an insurance broker that understand your business from a contractual and risk management standpoint. \*

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**Disclaimer:** *This article is written from an 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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# **No Recession?**

*From the DPIC Newsletter: DPIC e-Alert: Concerns About COAA*

From the looks of things, most design firms should remain smiling as the construction industry appears ready to move into its tenth year of expansion, albeit not at the rapid pace of growth enjoyed in 2000.

According to forecasters at F. W. Dodge, the value of construction projects is expected to increase another 1% this year, to \$468 billion. On the surface, one percent growth may not seem like much. But consider: the total volume is 86% higher than in 1992.

Projections for expansion are highest in non-residential and public work construction, while single-family housing is expected to decline slightly. Dodge points to highways and airports as big growth potential areas. Other healthy project types should include warehouses, office buildings, schools (especially higher education), mass transit facilities, churches, libraries, museums, aquariums and art galleries. Longer term, industrial plants should pick up steam over the next five years.

CMD Group predictions are not quite so rosy. They project a temporary 1.9% decline in 2001, followed by a 1.3% boost in 2002.

Meanwhile, ENR reports that Asia presents the hottest overseas market, led by strong construction in Japan and China. Most of Europe appears sluggish, although the U.K. appears strong.

Regardless of a boom or bust economy, project management is at the heart of the business of design. It provides the earnings engine that makes the entire enterprise thrive – or it can be the cause of the slow erosion of profits that weakens the health of the company. In DPIC Management Service Corporation's studies of highly profitable companies there is a consistent and statistically significant pattern: companies that commit to training in the process of project management do better than those that don't. "Effective Project Management Improves Profitability" can be found in DPIC's Loss Prevention Library at [www.DPIC.com](http://www.DPIC.com). \*