GREAT AMERICAN INSURANCE GROUP | Professional Liability

Great American's "Great 8, Plus 2"
Contract Check List

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Elevating Your Contract Review Game: Great American's Top Ten Contract Provisions

While Great American's Risk Management Team is committed to assisting you and your risk management needs, we have compiled a quick guide with key contract provisions that should be taken into consideration when reviewing your next contract.

1. Defense and Indemnification: You've heard it. You've seen it: "Design Professional will defend, indemnify and hold harmless the Client, the Contractor and all officers, directors, subsidiaries, parent companies, employees and agents from all losses and damages associated with this Project." This provision is frequently used by Owners and should be reviewed and revised to protect a design professional's interests.

Indemnification clauses are meant to shift the responsibility for certain potential risks from one project participant to another. However, it is important to know for what risks you are taking responsibility. As a design professional, you are only legally liable to indemnify another party for your own negligence. Nothing more, nothing less, which includes defense obligations (baring certain jurisdictions). Typically, professional liability policies do not cover defense costs of another party.

It is important to note that some contracts require the defense/indemnification of the Client for the Client's own negligence. Such contract provisions are enforceable in some jurisdictions. However, the language must be "clear and unequivocal." Despite the fact that this language would present coverage issues under the professional liability policy, the design professional can still be liable under the contract.

- ✓ Remember:
  - Limit the definition of "indemnitee" to only the party with whom you are contracting (example: terms such as "agent," "parent company," "subsidiaries" should be stricken from the contract).
  - Delete any defense obligations.
  - Indemnification obligation should be negligence-based only.

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A sample of an insurable indemnity provision:

> *To the fullest extent permitted by law, the Design Professional shall indemnify and hold harmless the Client from and against damages, losses, costs and expenses (including reasonable attorneys' and experts' fees, interest and court costs) to the extent such damages result from the negligent act, error or omission of the Design Professional, its employees, subconsultants or anyone for whose actions the Design Professional is legally responsible.*

2. **Standard of Care:** The standard of care is the standard by which a design professional's performance is judged. The industry standard is one of reasonableness and practicality. Remember, a design professional is providing a service, not a product, and the standard is not "perfection."

✓ Remember

- Words such as "above average," "highest," "best" and "first-class" delineate a higher standard of care and should not be the standard by which design professionals are judged. If you see these terms in your contract, it is best to remove them.
- Your professional liability insurance policy provides coverage for the industry standard. If your contract promises anything more, than that may present insurability issues.

A sample of an insurable standard of care provision is as follows:

> *The services that a Design Professional provides will be performed in a manner consistent with that degree of care as ordinarily exercised by similarly situated Design Professional currently practicing under similar circumstances. No warranty or guarantee is included or intended in this Agreement or instruments of its services.*

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3. **<u>"Time is of the essence"</u>:** Delete this provision if possible. This provision may invite potential delay claims later in the project. If any "milestone" dates are missed or any time provision in the contract is not carried out exactly, the other party has both the recourse of terminating the agreement and of bringing a claim for delay damages. Additionally, some courts have construed such a phrase as the establishment of an express warranty. It is our recommendation that this language be deleted from your contract.

4. **<u>Scope of Services</u>:** Be sure that your scope of services is specifically delineated in your contract. This means that the services you are providing *and not providing* should be defined in the contract. In addition, it is recommended that services being provided by other design professionals also be noted in this provision.

5. **<u>Incorporation by Reference:</u>** This is a biggie and is often overlooked. Essentially, this phrase is doing exactly what it says: it includes the terms and obligations of the underlying contract into the design professional's contract simply by mention. It is very common for consultant agreements to incorporate a prime agreement by reference. This language can present insurability/risk management issues as the prime agreement may contain inappropriate language for the consultant.

✓ Remember:

- If you see this provision, you should request a copy of the Prime agreement for review.

Sample language to include in your contract is as follows:

> *In the event of any discrepancy between the terms and conditions of the Consultant agreement and Prime agreement, the Consultant agreement will control.*

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6. **<u>Limitation of Liability:</u>** It is recommended that a Limitation of Liability provision be included in your contract. This provision, if found to be enforceable, can cap the potential damages that can be incurred[1].

✓ Remember:

- In order to enhance enforceability of such a clause, the design professional should draw the client's attention to the clause.
- Engage in negotiation with the client concerning the clause.
- Maintain documentation and evidence of that negotiation process.

Sample Language that can be used:

> *Notwithstanding any other provision of this agreement and to the fullest extent permitted by law, the Client agrees that the total liability, in the aggregate, of the Design Professional and the Design Professional's officers, directors, partners, employees, agents and consultants, to the Client and their respective officers, directors, employees, agents and anyone claiming by, through or under the Client for any and all injuries, claims, losses, expenses, damages whatsoever arising out of, resulting from or in any way relating to the Design Professional's services, this Agreement or any Addenda, from any cause or causes, shall be limited to [the proceeds of the Design Professional's available insurance coverage or the total amount of compensation received by the Design Professional, whichever is greater.*

[1] Limitation of liability clauses should be drafted by legal counsel in the design professional's jurisdiction with experience in this area. The phraseology of such clauses may be critical not only to their effectiveness and scope, but also to the enforceability of the clause itself, depending on wording and jurisdiction.

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DID YOU KNOW?

If your firm implements a limitation of liability of $250,000 or less in your contract, you may qualify for up to 15 percent reduction in premium with Great American Insurance Group.

7. **Alternative Dispute Resolution (ADR):** It is helpful to include an ADR provision in your contract, provided that this is negotiated with your client. At times, all that is needed is a meeting with your client to determine if the issue can be resolved in its initial stages. If this is not effective, "Mediation as a Condition Precedent" can be the next step. This essentially mandates the parties engage in mediation, with a neutral third party, to determine whether the issue can be resolved before any party can commence litigation.

A sample mediation clause to consider:

> *Design Professional and Client agree to submit all claims and disputes arising out of this Agreement to non-binding mediation before the initiation of legal proceedings. This provision shall survive the completion or termination of this Agreement; however, neither party shall seek mediation of any claim or dispute arising out of this Agreement beyond the period of time that would bar the initiation of legal proceedings to litigate such claim or dispute under the applicable law.*

In addition, you may often see an arbitration clause in your contract. It is highly recommended that these arbitration provisions are removed and replaced with a mediation clause. Arbitration lives up to its name and oftentimes the decision rendered is 'arbitrary.' In addition, arbitration is arguably more costly than litigation and the decisions are unappealable. Rather, mediation is the preferred method of resolution whereby a neutral party is retained to hear both sides of the conflict and the decision is non-binding. A mediation is a great avenue to explore a settlement before engaging in litigation and incurring legal fees.

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8. **<u>Ownership of Documents</u>**: Some contracts contain ownership clauses wherein the Client assumes ownership of the Design Professional's designs/specifications. While it is not recommended the ownership is transferred to the Client, there are ways to protect yourself if this becomes a 'deal-breaker.'

✓ Remember:

- All fees owed to the design professional must be paid in full before providing documents to the client.
- Ensure that an indemnification provision is included if the design professional is handing over their work product.

Sample Language is as follows:

> *Client agrees, to the fullest extent permitted by law, to indemnify and hold harmless the Design Professional and their respective officers, employees, agents and representatives, from any claim, damage, liability or cost (including reasonable attorney fees), caused by 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 specification from or through the Client without the written authorization of the Design Professional.*

9. **<u>Know Your Role and Avoid Express Warranties or Guarantees</u>**: The role of a Design Professional is often confused with that of a Contractor. The industry's standard of care for a design professional's performance is reasonableness and practicality, not perfection. Design Professionals provide a service, not a product. When referenced in a contract, your role should be defined as "Design Professional," "Architect," "Engineer," or "Consultant." If a client refers to you as a "Contractor" or "Subcontractor," it may indicate that the contract is more suited for a contractor doing work rather than a design professional providing services. A Design

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Professional cannot guarantee a perfect result, and it is recommended that any language referring to warranties or guarantees be removed.

- ✓ Watch for buzz words like "work," "warrants," "guarantees," "ensures," or "certifies" in your contract.

10. **Jobsite Safety**: Jobsite Safety has been and generally continues to be the responsibility of a Project's general contractor, unless stated otherwise. While this is a known obligation since the general contractor has control of the project site and those on-site, it is recommended that a Design Professional specifically exclude the any jobsite safety responsibilities in their contract.

We recommend adding the following language:

> The Design Professional shall not supervise, direct, or have control over Contractor's work. The Design Professional shall not have authority over or responsibility for the construction means, methods, techniques, sequences or procedures or for safety precautions and programs in connection with the work of the Contractor. The Design Professional does not guarantee the performance of the construction contract by the Contractor and does not assume responsibility for the Contractor's failure to furnish and perform its work in accordance with the Contract Documents.