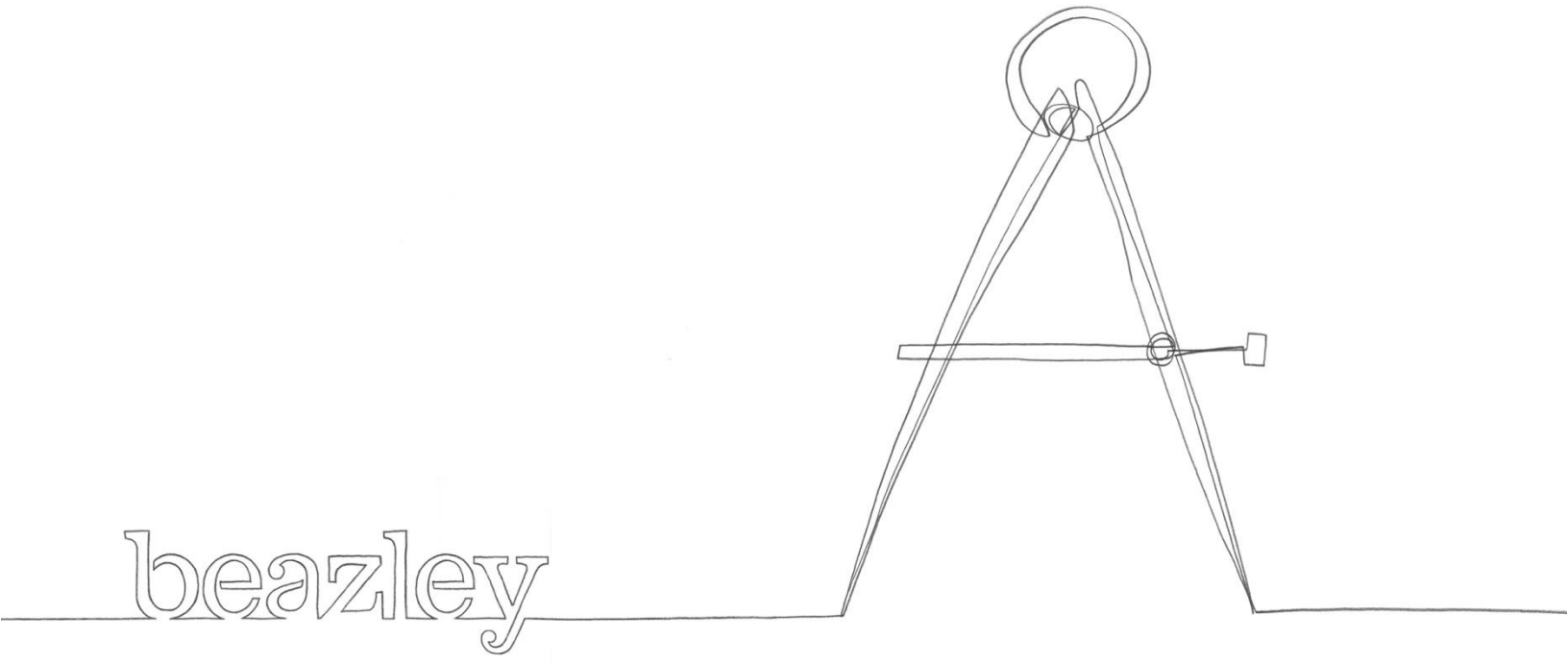
A&E Contract Review Guide



Contents

Introduction

As a broker for A&E professionals, you may be asked by design professionals to review their professional services agreements as they negotiate those agreements with their clients. Since the design professional is in a superior position to evaluate its business risks associated with the project, your review of such agreements is likely from a risk management and professional liability perspective. The purpose of this document is to provide an overview of the more important steps to take and the provisions on which to focus when reviewing agreements on behalf of a design professional. Although every contract is different and every project has unique risks, this document highlights the critical areas of concern from a risk management and professional liability perspective.

Why is a written contract important?

We recommend a design professional have a written, executed professional services agreement prior to beginning services on each project. Some design professionals and clients are hesitant to have a written agreement and rely on oral agreements, particularly if they have a long working relationship. These design professionals argue that a written contract seems like they don't trust the client and they "have always" relied on a handshake to close the deal for a project. This approach is dangerous. We strongly discourage oral agreements since they do not provide any protections to the design professional. While the parties may be in perfect agreement regarding the expectations at the beginning of a project, memories are certain to fade and change if there are problems during the project. In claims situations, oral agreements quickly deteriorate into a "he said, she said" fight and the design professional has no document upon which to rely.
In short, oral agreements are not worth the paper they are written on.

A design professional's contract with its client is perhaps the most critical document in a construction project because it defines the parties' responsibilities and rights in connection with the project. The contract should guide the parties as the project proceeds through completion and, in the event of a dispute, may be the first line of defense for a design professional depending on the negotiated terms and conditions. The contract negotiation phase sets the tone for the design professional's relationship with its client and allows the design professional an opportunity to evaluate its vulnerability in the project. The negotiation is the time to assess and manage the client's expectations and, if the client has unreasonable expectations, educate the client regarding the design professional's customary role and the value of the design professional's services on the type of project contemplated.

Preliminary issues when the contract first lands on your desk

Before diving into the agreement to evaluate the substantive terms and conditions, it helps to take a quick look at the agreement to assess the following:

On whose behalf are you reviewing the agreement?

This question is particularly important if presented with an Architect/Consultant agreement since both parties are design professionals. Your risk management recommendations will be different depending on whether you are evaluating the agreement from the Architect's or the Consultant's standpoint. Although you may generally review agreements from the party that will provide the services (i.e., the Consultant in an Architect/Consultant agreement), you may be asked to review agreements from the party that is requesting the services (i.e., the Architect in an

Architect/Consultant agreement). It may be useful to think of these as "reverse contracts" because it reinforces that you are reviewing the agreement from the standpoint of the professional retaining the consultant. Note, this document does not address "reverse contracts"; rather, it looks at the risks associated with agreements from the perspective of the design professional that will provide the services. It is good practice to state in your suggested revisions from whose perspective you have reviewed the agreement, particularly if the names of the Architect or Consultant have not been properly filled in.

How does the agreement designate the design professional?
Most agreements will define and designate a title to the parties on the first page of the agreement. You may wish to recommend that design professionals be referred to as "Design Professional"; "Consultant"; "Architect"; or "Subconsultant" as opposed to "Contractor" or "Subcontractor" since the former designations more accurately reflect design professionals' status and their role of providing professional services, as opposed to the latter designations which reflect the role of general contractors. It is often a tip-off that the agreement may not be appropriate for a design professional if the client uses the designation "Contractor" for the design professional.

Once the parties are defined, make sure the designations are consistently applied throughout the agreement and exhibits.
Consistency and clarity may be vital if a trier of fact is required to analyze the agreement and determine enforceability.

Has the agreement been executed?
If so, it will be much more difficult to negotiate changes that are favorable to the design professional.

What is the date on the agreement?
The agreement execution date is usually found on the first page and again on the execution page above the signature blocks. If the agreement is not signed by the parties, but the date in the agreement is months, or sometimes even years, prior to the date you are reviewing the agreement, you may want to follow up with the design professional to inquire whether services have been provided. Sometimes a project is well underway, or even completed, but the parties have not executed the contract. In some instances, the design professional may have completed its services and the client demands the design professional sign the contract prior to paying the design professional for services rendered. This scenario puts the design professional in a difficult position if the agreement includes onerous provisions since the client has no incentive to negotiate the agreement once the services have been provided.

It's time to attack the contract!

Once you have considered the preliminary issues above, you can move on to the substantive terms and conditions. It's important to remember that reviewing and negotiating contracts is not an exact science and two people may review the same contract and have slightly different, yet still appropriate, recommendations for the design professional. While the reviewers may suggest different modifications to the same provision, as long as the revisions will effectively manage the design professional's risk on the project, both may be "correct" revisions.

The "Big 6" Provisions:

It makes sense to discuss the most critical provisions first, since design professionals may ask you to identify the "deal breakers" in their contract. From a risk management and professional liability perspective, the most critical provisions are as follows (in alphabetical order):

1. **Certifications, Guarantees, and Warranties**
2. **Dispute Resolution**
3. **Incorporation by Reference of another Contract or Document**
4. **Indemnity Obligation to Client**
5. **Instruments of Service**
6. **Standard of Care**

1. Certifications, Guarantees, and Warranties

Design professionals should not give warranties, guarantees or certifications of their services. It is typical for suppliers of goods to provide various warranties. Thus, clients often expect design professionals to provide them as well. Clients may need to be educated that the role and standard of care for design professionals is distinct from that of suppliers of goods. Design professionals provide services (not goods) and should be held to a negligence-based standard of care that is guided by what a reasonable design professional would do under similar conditions. Language requiring the design professional to guarantee or warranty services may inappropriately elevate the standard of care to a perfection standard.

The AIA documents address certificates and provide that the design professional is not required to execute certificates or consents that would require knowledge, services or responsibilities beyond the scope of the agreement. In addition to the AIA language, we recommend deleting words such as "guarantee"; "warrant"; "ensure"; and "certify" with respect to design professional's services. If the client requires the design professional to provide certifications for the project, we recommend tying the certification to the generally accepted professional standard of care and modifying the language to certify "to the best of the design professional's information, knowledge, and belief".

Tips to keep in mind:

- Delete guarantees and warranties
- If have to give a certification, modify with language such as "to the best of Design Professional's knowledge, information, and belief" or "in Design Professional's opinion"
- Avoid use of words such as "all"; "every"; "insure"; "ensure"; "assure"
- Do not certify contractor built in compliance with code or in strict accordance with plans and specifications (modify to include "in general" compliance and "to the best of Design Professional's knowledge, information, and belief")
- Do not certify project will achieve any particular LEED standard or sustainable design goal

2. Dispute Resolution

Mediation before litigation preferred for domestic projects

We generally recommend a dispute resolution provision requiring non-binding mediation as a condition precedent to litigation. An example of such language is as follows:

> *"Prior to the initiation of any legal proceedings, the parties agree to submit all claims, disputes or controversies arising out of or in relation to the interpretation, application or enforcement of this Agreement to non-binding mediation. Mediation shall be conducted under the auspices of the American Arbitration Association or such other mediation service or mediator upon which the parties agree. The party seeking to initiate mediation shall do so by submitting a formal written request to the other party to this Agreement. This Article shall survive completion or termination of this Agreement, but under no circumstances shall either party call for mediation of any claim or dispute arising out of this Agreement after such period of time as would normally bar the initiation of legal proceedings to litigate such a claim or dispute under the applicable law."*

Mediation allows the parties the opportunity for a creative dispute resolution process that is confidential, voluntary, and non-binding. Unfortunately, clients sometimes prefer arbitration as the binding dispute resolution mechanism. There are numerous drawbacks to arbitration, including little or no discovery or rules of evidence and no rights to appeal. More so than in a courtroom setting, the parties are subject to the whims of the arbitrators. If the client insists on arbitration as the binding dispute resolution procedure, we recommend requiring limited discovery proceedings and adherence to the rules of evidence, and limiting the scope of arbitration to claims less than a certain dollar threshold such as $100,000.

Who should pay for the dispute resolution proceedings?

The American Rule and English Rule address the assessment of attorney's fees arising out of litigation. Generally speaking, under the American Rule each party is responsible for paying its own attorney's fees and the attorney's fees are not awardable to the wining party, unless statutorily or contractually authorized. In contrast, the English Rule provides that the party who loses in court will pay the other party's attorney's fees. The rationale for the English Rule is that a litigant (whether plaintiff or defendant) is entitled to legal representation and, if successful, should not be left out of pocket by reason of his or her own legal fees.

With increasing frequency, design professionals' contracts include attorney-fee-shifting clauses. These provisions are typically worded as follows: "In the event that the Client or Design Professional shall retain the services of an attorney in order to bring a legal action against the other, including any action for non-payment or breach of this Agreement, the Client and Design Professional agree that the prevailing party shall be entitled to recover from the non-prevailing party its costs of enforcing or defending same, including but not limited to, reasonable attorney's fees, expert witness fees and court costs."

At a minimum, design professionals should delete any provisions that are drafted unilaterally in favor of the client that allow only a prevailing client to recover legal expenses from the design professional. Further, we generally recommend design

professionals delete even mutually drafted prevailing party provisions that allow either party to recoup attorney's fees if they prevail. From a business standpoint, these provisions may be beneficial in the event a design professional prevails in litigation. However, these provisions may be problematic from an insurability perspective. In the event the design professional is obligated to reimburse the client, there may be a coverage issue with the design professional's professional liability insurance because, absent the contract provision, there would be no obligation for the design professional to pay for the client's fees and costs.

Tips to keep in mind:

- Recommend non-binding mediation as a condition precedent to litigation
- Discourage the use of arbitration
- If Client insists on arbitration, require some limited discovery and adherence to the rules of evidence and limit the scope of arbitration to those claims that do not exceed $100,000, inclusive of interest and attorney's fees
- If Client insists on arbitration, require both parties' consent to any joinder and consolidation
- If Client insists that a design professional agree to be joined as a party to an arbitration between the client and a third-party, qualify that such joinder is conditioned upon the design professional having the opportunity to fully participate in the arbitration, including the selection of arbitrators
- Delete attorney's fee shifting provisions

3. Incorporation by Reference of another Contract or Document

Danger! Danger!

It is not uncommon for a consultant agreement to incorporate by reference a prime agreement between the consultant's client and the owner. Not only do we frequently see these "incorporation by reference" provisions in client generated contracts, but both the 1997 and 2007 editions of the AIA Standard Form of Agreement between Architect and Consultant incorporate the Prime Agreement between the Owner and Architect. (See, AIA C141-1997, Article 2.1; AIA C401-2007, Article 1.1).

Incorporating any document by reference may create significant risk management and liability issues for the consultant. When a consultant agreement incorporates any document by reference, it is imperative that the consultant obtain and review the document to ensure the document does not contain inappropriate language that may raise the consultant's standard of care or include provisions that may create insurability issues, such as an inappropriate indemnity provision or warranties or guarantees. Incorporating a document by reference effectively makes the document a part of the consultant agreement with the same force and effect as the provisions in the consultant agreement. If the consultant's client refuses to provide the documents it seeks to incorporate, the consultant should not execute the consultant agreement.

How to deal with incorporation by reference

We recommend adding language to the consultant agreement clarifying that in the event of any discrepancy between the terms and conditions of the consultant agreement and the prime agreement (or other document incorporated by reference), the consultant agreement will control. Although the AIA C141-1997 merely states that the prime agreement is "made a part of" the consultant

agreement, the AIA C401-2007 provides protection to the consultant by specifically stating that the consultant agreement shall govern if a provision of the prime agreement conflicts with a provision of the consultant agreement.
If the client refuses to include language allowing the consultant agreement to take precedence over the prime agreement, the consultant has two options: either specifically list in the consultant agreement those provisions contained in the prime agreement that the consultant does not agree to incorporate, or specifically list in the consultant agreement those provisions in the prime agreement that the consultant does agree to incorporate. From a risk management perspective, we recommend listing those provisions the consultant agrees to incorporate. If the consultant lists only the objectionable provisions, the consultant risks the possibility of missing an onerous provision and thereby inadvertently agreeing to that provision in its consultant agreement.

Tips to keep in mind:

- If Client incorporates any document by reference, review and confirm the terms and conditions of that document are acceptable and consistent with the Consultant Agreement
- Include provision in Consultant Agreement that in the event of discrepancy between the documents, the Consultant Agreement shall govern
- If Client refuses to allow the Consultant Agreement to govern, list in detail in the Consultant Agreement which provisions of the referenced document are not incorporated OR list in detail those provisions that the Consultant agrees are incorporated (Note, this is risky and requires thorough review and evaluation of referenced document)

4. Indemnity Obligation to Client

Design professional's indemnity obligation must be negligence-based!

Indemnity is an agreement whereby one party agrees to assume the liability of another in the event of a loss. Indemnity provisions can be very difficult to negotiate and have far reaching implications. While the concept of making the client whole for losses caused by the design professional is rational, too often the provisions are "one-sided" in favor of the client and require the design professional to assume the liability of the client regardless of actual fault. Design professionals should reject these broadly written indemnity provisions and revise them so the indemnity obligation is limited to the extent the damages are caused by the design professional's negligent performance of services under the agreement. If the indemnity provision is not appropriately negligence-based, the design professional may be exposed to liability beyond that for which it is insured.

Indemnifying for intent-based actions:
As noted in the previous section, it is critically important to ensure the indemnity provision is negligence-based. Including language requiring the design professional to indemnify for its "recklessness, wrongful acts, intentional misconduct, willful misconduct and gross negligence" (or some combination thereof) potentially exposes a design professional to a liability beyond that for which it is insured.

These words are problematic because they have an element of intent and are not negligence-based. Deleting language requiring the design professional to indemnify for its "gross negligence" may be particularly troublesome since "negligence" is referenced, but keep in mind that Black's Law Dictionary defines

"gross negligence" as the "intentional failure to perform" a duty, thus clearly establishing an element of intent which is beyond coverage contemplated by professional liability insurance.

Indemnifying for breach of contract:

These days, clients are including "breach of contract" among the laundry list of circumstances under which the design professional is required to contractually assume a duty to indemnify. From a risk management and professional liability standpoint, language requiring the design professional to indemnify for its breach of contract creates a significant additional exposure. Arguably, most third-party claims will arise out of a performance-based issue by the design professional and will boil down to assertions that because the design professional breached the contract, the design professional failed to meet the applicable standard of care and was negligent, thus triggering the professional liability insurance policy. Further, from a business standpoint, asserting during contract negotiations that the design professional has no obligation to indemnify the client if it breaches (or certainly if it "materially breaches") its contract may not pass the "laugh test" and a design professional will be hard pressed to convince the client that it has no indemnity obligation to the client under a breach of contract scenario.

That being said, if a breach of contract claim does not arise out of the design professional's performance, the design professional's contractual obligation to indemnify the client for breach of contract may be beyond the coverage provided by a negligence-based professional liability insurance policy.

Limiting the definition of "Indemnitees":

It is prudent for design professionals to limit the indemnified parties to the design professional's client, and the client's employees, officers, and directors. We typically recommend deleting broad and undefined terms such as the client's "agents"; "attorneys"; "insurers"; "parent company"; "subsidiaries"; "related and affiliated companies"; "assigns"; "lenders"; "contractors"; and "subcontractors" from the "Indemnitees" definition since it may be impossible to determine with any degree of certainty who would fall into those categories at the time of contract negotiations.

Jurisdictions vary in their interpretation of whether a design professional owes a duty of care to another party with whom the design professional has no contract, based in large part on the application of the economic loss doctrine, which is why design professionals commonly seek to negotiate language in the agreement expressly stating there are no third party beneficiaries. In addition to negotiating a "No Third Party Beneficiaries" provision, design professionals commonly seek to delete third parties (such as the client's contractors, consultants, lenders, insurers, attorneys, etc.) from the "Indemnitees" definition in any indemnity provision. These third parties are not directly part of the client entity and the design professional does not (and should not) owe them the same duties it owes its client with whom the design professional has a contract. In the event any of these third parties are damaged by the design professional (including damages caused by the design professional's negligence) they can seek remedies to the extent any remedies are available at law.

By specifically including third parties in the "Indemnitees" definition, these parties may establish a third-party beneficiary status, at least with respect to the indemnity provision. In fact, some contracts include "Third Party Beneficiaries" provisions that have language along the lines of, "Except with respect to the indemnity obligations, there are no third party beneficiaries to this agreement."

By including the third parties in the "Indemnitees" definition in the indemnity provision, combined with the Third Party Beneficiary language as noted above, any protections afforded under the economic loss doctrine may be lost and the design professional could owe these parties an indemnity obligation. In the event the design professional is called upon to indemnify these third parties, there may be a coverage issue with the design professional's professional liability insurance because, absent the contract language, there may be no obligation for the design professional to indemnify those parties.

What about the duty to defend?

We recommend deleting any language in the indemnity provision requiring the design professional to defend the client. The word "defend" raises significant insurability issues, regardless of the insurance company involved. The duty to defend is problematic because it is broader than the duty to indemnify. Accordingly, when a design professional has a duty to defend, the design professional may be required to defend a claim based upon a mere allegation of negligence, unlike a duty to indemnity which is trigged by actual negligence. The duty to defend a client may be interpreted as a contractual obligation rather than an obligation triggered by adjudication of the design professional's negligence. As a contractual obligation, the duty to defend would not be covered by the design professional's professional liability insurance policy.

Mutual indemnity provisions

We are sometimes asked whether it is better for a design professional to have a mutual negligence-based indemnity provision or no indemnity provision at all in a professional services agreement. From a risk management and liability perspective, even if a mutual indemnity provision is appropriately negligence-based such that each party's indemnity obligation is limited to the extent the damages are caused by the party's negligence, the design professional is in a better position if it has no indemnity obligation to the client. Generally speaking, a mutually drafted indemnity provision tends to benefit the client more than the design professional since the client is more likely to be in a position to seek indemnity from the design professional since the client is vicariously liable for the negligence of the design professional. If the design professional has the option of deleting a mutual indemnity provision and having an agreement that does not require the design professional to have any indemnity duty toward the client, we recommend deleting the mutual provision.

Tips to keep in mind:

- Delete duty to defend
- Delete "claims"; "suits"; "causes of action"; "actions"; "demands"; "allegations" since these words suggest a duty to defend
- Limit the indemnity obligation "to the extent damages are caused by the design professional's negligence"
- Avoid broad definition of Indemnitees and limit the indemnity obligation to the Design Professional's Client, the Client's employees, officers, and directors and delete "agents"; "parent company"; "subsidiaries"; "related and affiliated companies"; "assigns"; "lenders"; and "subcontractors"
- Limit the indemnity obligation to Design Professional and the Design Professional's consultants for whose actions the Design Professional "is legally responsible" and delete language obligating the Design Professional to indemnify for the actions of those for whom the Design Professional "may be liable" and those whom the Design Professional "directly or indirectly retained"

5. Instruments of Service

The Basics

We recommend the design professional maintain sole ownership of its work product, regardless of whether the work product is in hard copy or electronic form. Although maintaining ownership of the work product is not necessarily a deal breaker from a risk management and professional liability perspective, the design professional should insist on payment for services rendered prior to transferring ownership of its work product, limit the client's use of the work product to completion and use of the project, and insist on indemnity protection in the event of unauthorized use of the documents. An example of a provision incorporating these concepts, is as follows:

> *"All reports, notes, drawings, specifications, data, calculations, and other documents, including those in electronic form, prepared by Design Professional are instruments of Design Professional's service that shall remain Design Professional's property. The Client agrees not to use Design Professional-generated documents for marketing purposes, for projects other than the project for which the documents were prepared by Design Professional, or for future modifications to this project, without Design Professional's express written permission. Any reuse or distribution to third parties without such express written permission or project-specific adaptation by Design Professional will be at the Client's sole risk and without liability to Design Professional or its employees, subsidiaries, independent professional associates, subconsultants, and subcontractors. Client shall, to the fullest extent permitted by law, defend, indemnify, and hold harmless Design Professional from and against any and all costs, expenses, fees, losses, claims, demands, liabilities, suits, actions, and damages whatsoever arising out of or resulting from such unauthorized reuse or distribution."*

What about electronic documents?

As with hard copies, if a client insists on access or ownership of a design professional's electronic documents, we recommend insisting on payment for services rendered prior to transferring ownership of electronic work product, limiting the client's use of the electronic work product to completion and use of the project, and insisting on indemnity protection in the event of unauthorized use of the electronic documents. In addition, electronic documents present special concerns to design professionals due to the possibility of alteration of the electronic documents and the client's desire to rely upon them as contract deliverables. If the client demands the design professional's electronic documents, we recommend additional language stating that the electronic documents are provided to the client for convenience and informational purposes only and not as an end-product, and that they do not constitute "Contract Documents."

Copyright considerations

With increasing frequency, clients are seeking transfer of the copyright of the design professional's work product. While we discourage transfer of copyright to the client, the design professional should insist on language clarifying that such transfer does not impair the design professional's future use of its standard design details. If the client seeks copyright of the design professional's work product, you may wish use to use language such as the following:

> *"Notwithstanding any other provision in this Agreement, the Design*

Professional shall not be in violation of this Agreement if the Design Professional utilizes any standard details that may be incorporated into the work product generated by the Design Professional in connection with this Project. The Client understands that regardless of any transfer of ownership or copyright rights granted to the Client pursuant to the terms of this Agreement, the Design Professional shall in no way be restricted or prohibited from future use of any such standard details."

What if a third party wants the design professional's documents?

Design professionals are sometimes asked to provide their documents to a third party with whom they have no contract as an accommodation to the design professional's client. Design professionals often want to comply with the client's request in an effort to maintain the client relationship. However, handing over its documents may pose significant liability issues for the design professional, particularly in instances where the design professional provided reports (such as feasibility studies) and significant time has elapsed between the design professional's performance of services and the third-party request for the documents.

We recommend the design professional obtain a release and indemnity agreement from the third party before providing the documents. If the third-party refuses to provide the agreement, then the design professional should refuse to provide the documents. In addition, the design professional should put waiver and release language right on the documents themselves, and remove all stamps and signature blocks. Finally, we recommend the design professional consult with a local attorney to discuss any licensure issues.

Based on the foregoing commentary, we recommend the design professional incorporate indemnity language such as the following into a letter to the third party:

"This is to confirm that we have agreed to provide you [at no cost / for $_____] with certain documents prepared by us for your use. You recognize that data, plans, specifications, reports, documents or other information recorded on or transmitted as electronic media are subject to undetectable alteration, either intentional or unintentional due to, among other causes, transmission, conversion, media degradation, software error, or human alteration. Accordingly, the electronic documents provided are for informational purposes only and are not intended as an end-product. It is understood and agreed that the documents provided were prepared for another client specific to that client's needs, budget, time constraints and site constraints. We make no representations or warranties, either expressed or implied, regarding the suitability of the documents for your intended purposes or applications. Any use or reuse of our documents will be at your sole risk and without any liability or legal exposure to us. Further, you agree to waive any and all claims against us and release, defend, indemnify, save and hold us harmless from and against all claims, losses, liabilities, demands, and damages arising out of or resulting from the use, reuse or alteration of our documents by you or anyone to whom you provide the documents. Upon execution of this letter below, we will provide you with a copy of the documents in pdf format."

In addition, we recommend including language such as the following on the documents themselves:

> *"These documents have been provided as an accommodation to [third party]. It is understood and agreed that these documents were prepared for another client specific to that client's needs, budget, time constraints and site constraints. No verification has been made regarding the suitability of the documents for any other purpose or application. Any use of the documents is at your sole risk. Use of the documents in any way shall constitute an acknowledgement and acceptance of the foregoing."*

Tips to keep in mind:

- Try to maintain copyright and ownership
- Limit Client's use of instruments of service to the completion, use, and occupancy of the current project
- Any reuse without written consent of Design Professional on other projects or modifications to the current project should be at Client's risk without liability or legal exposure to Design Professional
- Include document defense and indemnity protection running in favor of Design Professional for re-use and modification of instruments of service, regardless of whether Design Professional transfers ownership rights to Client
- If Client requests electronic documents, include language that electronic documents may be unintentionally altered; are for informational purposes only and not intended as an end product; Design Professional makes no warranties regarding fitness or suitability; and Client will defend and indemnity Design Professional for claims relating to unauthorized use, reuse, or alteration of the electronic documents

6. Standard of Care

The standard of care is the standard by which a design professional's performance is judged. The standard is not one of perfection. Rather, the standard is negligence-based and guided by what a reasonable, practicing design professional would do under similar conditions. We recommend design professionals include a standard of care provision in every agreement, as follows:

> *"The Design Professional's services shall be performed in a manner consistent with that degree of skill and care ordinarily exercised by practicing design professionals performing similar services in the same locality, at the same site and under the same or similar circumstances and conditions. The Design Professional makes no other representations or warranties, whether expressed or implied, with respect to the services rendered hereunder."*

The design professional should diligently monitor standard of care language and be wary of any client's attempts to modify the standard with warranty or guarantee language. Any language calling for the design professional's "best services"; "highest degree of skill and care"; "first-class services"; "first-rate services"; or "technical accuracy" should be stricken since these words may inappropriately elevate the standard of care.

Although language calling for the design professional's "first-class services" or "first-rate services" should be stricken, sometimes clients refuse to do so. Under these circumstances, choice of law provisions can prove extremely important because jurisdictions likely vary in their interpretation of such language. If case law in the state governing the agreement has interpreted such language to establish a basis for a breach of warranty cause of action, such language would present coverage issues under professional liability insurance. If the client steadfastly refuses to delete

the offending language, we recommend adding language that states: "With respect to any professional services rendered under this Agreement, nothing herein shall be construed as holding the Design Professional to a standard of care that is more stringent than the generally accepted standard of professional skill and care ordinarily exercised by similarly situated professionals."

Tips to keep in mind:

- Make sure reasonable and negligence-based
- Should be limited to the skill, care, and judgment ordinarily exercised by similarly situated design professionals performing same services
- Delete any guarantees, warranties, and certifications
- Delete language that elevates standard of care beyond ordinary, reasonable standard, such as "highest"; "best"; "first-class"; "first rate"
- Delete "to the satisfaction of the client"; "in the client's sole judgment"; "non-negligent manner"

You've tackled the "Big 6", now what?

The "Big 6" are the provisions that, at a minimum, must be dealt with in a design professional's contract with its client. Of course, the contract will include many other terms and conditions that a prudent review should address. We discuss some of the more common provisions (in alphabetical order), and tips to keep in mind when looking at these provisions, below:

Agreed Remedies to Limit Design Professional's Liability

Limitation of liability provisions drafted in the design professional's favor are very beneficial because they contractually limit the design professional's liability to its client to a specific dollar amount or measurable threshold. Options include limiting the design professional's liability to the total fee, the amount of insurance available, or some arbitrary amount upon which the parties agree. We generally recommend language such as the following:

> *"To the fullest extent permitted by law, the total liability, in the aggregate, of Design Professional and Design Professional's officers, directors, employees, agents, and consultants to Client and anyone claiming by, through or under Client, for any and all injuries, claims, losses, expenses, or damages whatsoever arising out of or in any way related to Design Professional's services, the Project or this Agreement, from any cause or causes whatsoever, including but not limited to, negligence, strict liability, breach of contract or breach of warranty shall not exceed the total compensation received by Design Professional under this Agreement, or the total amount of $_____, whichever is greater."*

Clients often will not accept these types of provisions. However, for certain projects, such as casino projects and limited scope projects such as peer reviews, they represent fair and equitable risk allocation because the realistic exposure to the design professional far outweighs the reward. States vary as to whether they will enforce these provisions and clients may assert that the provisions are unenforceable because they "are against public policy" or the client did not understand or know the provision was present in the agreement. Obviously, the design professional will want to be familiar with the applicable state law's position regarding enforcement of limitation of liability provisions. We also recommend the provision be conspicuously placed in the agreement to thwart client arguments that

the client was unaware of the provision. The design professional may also consider requiring the client initial its acceptance of the provision in the agreement, although such verification cuts both ways because the client may then refuse to accept the highlighted provision.

Tips to keep in mind:

- Particularly important when Design Professional's fee is relatively low
- Limit to Design Professional's fee or amount parties agree upon
- Limitation should broadly include Design Professional's officers, directors, employees, agents, and consultants
- Limitation should broadly include all causes of action, including but not limited to, negligence, strict liability, breach of contract or breach of warranty
- Be aware of any exceptions to the application of the provision which may weaken the limitation of liability

Assignment

Clients often include one-sided assignment provisions that preclude the design professional from assigning the professional services agreement, but grant unrestricted rights of assignment to the client. It may well be reasonable for the client to limit the design professional's right to assign the agreement; after all, the client specifically selected the design professional to perform the intended services. Contrastingly, a design professional may not be able to prevent or limit a client's right to assign the agreement to a new client or its lender, but a new client or lender should not be allowed greater rights under the contract than the original client.

We recommend reserving the design professional's right to refuse to execute documents that the design professional determines might increase its contractual or legal obligations or the availability or cost of its professional or general liability insurance in the event the client assigns the agreement, such as the following:

> *"The Design Professional shall not, in connection with any such assignment by the Client, be required to execute any documents that in any way might, in the sole judgment of the Design Professional, increase the Design Professional's contractual or legal obligations or risks, or the availability or costs of its professional or general liability insurance."*

This reservation of rights language is particularly important if a lender requests the design professional to execute certifications or warranties for the project. We have encountered issues when the assignment provision in a contract broadly states that the design professional will execute any and all certifications requested by a lender and then the lender requests the design professional to execute inappropriately worded certifications (for example, that the building was designed and constructed in compliance with all applicable laws, codes, and ordinances, including the American with Disabilities Act or that the building was constructed in strict accordance with the design professional's plans and specifications). Obviously, the design professional cannot make these types of unqualified certifications. However, the design professional may be subject to a breach of contract claim if it refuses to execute the certifications as requested based on broad assignment language in the contract if there are no limitations to the design professional's obligations.

Tips to keep in mind:

- Assignment by either party acceptable with consent of the other party
- Try to qualify that Client's consent to assignment by Design Professional should not be unreasonably withheld
- If Client has right to assign the Agreement, add language that the Design Professional does not have to execute any documents that might increase Design Professional's contractual or legal obligations or the availability or cost of its professional or general liability insurance

Code and Law Compliance

Design professionals do have a duty to comply with laws, codes, and regulations when providing professional services. However, clients often insist that design professionals comply with "all" laws, codes, and regulations. Inserting the word "all" is problematic from a risk management and liability perspective due to the probability of conflicting laws, codes, and regulations and the overwhelming, if not impossible, task of discovering, reviewing, and complying with "all" laws, codes, and regulations.

The solution to this problematic language is to tie the design professional's duty to comply with laws, codes, and regulations to the standard of care. We recommend deleting "all" and replacing with "applicable". In addition, we recommend adding language stating that the design professional will exercise its professional skill and care consistent with the generally accepted standard of care to provide a design that complies with such regulations and codes, but that the design professional does not warrant that all documents issued by it shall comply with the regulations and codes.

Tips to keep in mind:

- Agree to comply with "applicable" codes and regulations in accordance with standard of care, not "all" codes and regulations
- Include language that Client recognizes possibility of various, and possible contradictory, interpretations of codes and regulations
- Delete warranties

Confidentiality

Clients often insist on provisions requiring the design professional not to disclose the client's confidential information. Even the 1997 AIA Owner/Architect agreements require the Architect to keep the Owner's information confidential except under certain defined circumstances. The 2007 AIA agreements follow suit, but eliminate many of the exceptions. The requirement to maintain the client's confidential information is acceptable as long as the duty is not absolute. To avoid a breach of contract allegation, we recommend clarifying that the confidentiality provision does not restrict the design professional from disclosing the information if the information is in the public domain, if disclosure is required by law, or if disclosure is reasonably necessary for the party to defend itself from any suit or claim.

Tips to keep in mind:

- Ensure Design Professional's obligation to maintain confidential information is not absolute
- Include exceptions if information is in public domain; if disclosure is in compliance with legal orders; and if disclosure is reasonably necessary for Design Professional to defend itself in a claim

Construction Phase Services

Jobsite safety:
The design professional should not assume any contractual responsibility for jobsite safety. The contractor is in charge of the project jobsite and has actual control of the site and those on the site; therefore, the contractor should be solely responsible for jobsite safety. We recommend including language explicitly disclaiming responsibility for the contractor's means, methods, sequences, and safety procedures, such as the following:

> *"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."*

What if you see a dangerous condition while at the jobsite?
Design professionals often seek guidance when they observe what they perceive as an extreme safety hazard on the jobsite while performing construction phase services. From a risk management and professional liability perspective, the concern is that if a design professional gets involved with an imminently dangerous safety condition, a plaintiff may argue the design professional has broad responsibilities for ensuring appropriate jobsite safety programs and precautions are in place in the event of a personal injury on the jobsite.

Give Verbal Notification at Jobsite:
While a design professional should not have a legal duty regarding jobsite safety, she or he arguably does have an ethical duty to respond in the event she or he observes a condition that constitutes an imminently dangerous condition. A design professional should not actively look for safety issues while on the jobsite; however, if she or he sees an obvious and dangerous condition that threatens life safety, she or he should immediately alert the person in charge of the jobsite of the condition. This notification should be limited to the objective facts as observed and should not include any recommendations regarding remedying the condition.

Send Written Communication:
The design professional should follow up the jobsite notification with a written communication to the contractor and project owner reporting the observation. As with the verbal notification at the jobsite, this letter should be brief and include objective observations, not recommendations or advice. We recommend the letter reiterate the language in the contract that the design professional does not supervise, direct, or have control over the contractor's work and does 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.

Stick to your Scope of Services:
Finally, the design professional should not make a special trip back to the jobsite to check whether the safety issue has been corrected. Well-drafted contract language disclaiming liability for jobsite safety can be undercut if a design professional takes on extra-contractual duties that are not included in the design professional's scope

of services. This is an important point: even if a design professional's agreement includes appropriate language disclaiming responsibility for jobsite safety, if the design professional performs jobsite safety tasks (such as attending regular contractor safety meetings, making recommendations regarding safety, or following up to check on a safety condition observed during construction phase services) those actions could be construed as evidence that the design professional had an integral role in, and responsibility for, jobsite safety which would undermine the contract language.

Shop drawing stamp language:
We recommend a design professional's shop drawing stamp contain language mirroring that found in the standard AIA Owner / Architect agreements. In particular, the stamp should state that the review is only for general conformance with the contract documents and is not conducted to determine accuracy of details. The language below is an example of appropriate shop drawing stamp language:

DESIGN PROFESSIONAL'S REVIEW

___NO EXCEPTIONS TAKEN
___MAKE CORRECTIONS NOTED
___REJECTED
___REVISE AND RESUBMIT
___SUBMIT SPECIFIED ITEM

SUBMITTAL WAS REVIEWED ONLY FOR GENERAL CONFORMANCE WITH THE INFORMATION GIVEN IN THE CONTRACT DOCUMENTS. IT IS NOT CONDUCTED FOR THE PURPOSE OF DETERMINING THE ACCURACY OF DETAILS SUCH AS DIMENSIONS AND QUANTITIES, OR FOR SUBSTANTIATING INSTRUCTIONS FOR INSTALLATION OR PERFORMANCE OF EQUIPMENT OR SYSTEMS. CONTRACTOR REMAINS RESPONSIBLE FOR THE ACCURACY OF CONTENT IN SUBMITTED DOCUMENTS, COORDINATION OF HIS WORK WITH OTHER TRADES AND CONFIRMING AND CORRELATING DIMENSIONS AT THE JOB SITE. THE REVIEW SHALL NOT CONSTITUTE APPROVAL OF SAFETY PRECAUTIONS OR CONSTRUCTION MEANS, METHODS, TECHNIQUES, SEQUENCES OR PROCEDURES.

Stop work authority
The design professional should not have the authority to stop the contractor's work and should refuse any effort to delegate such authority to the design professional. Not only is there potential liability to the contractor if the design professional wrongfully stops the work, it can open the design professional up to potential exposure under the Occupational Safety and Health Administration (OSHA). OSHA review commissions have cited authority to stop the work as a factor in finding design professionals liable for site safety issues. However, the design professional may assume the authority to reject work as part of its construction phase services. The AIA documents include appropriately worded provisions granting the design professional authority to reject work that does not conform to the Contract Documents.

Distinct from the authority to stop work is the ability (or duty) to reject work. Many contracts, including the AIA documents, authorize the design professional to reject (but not stop) the contractor's work that does not conform to the Contract Documents based on the design professional's site observations during the Contract Administration phase. However, the AIA provides protection to the design professional by clarifying that the authority to reject work does not give rise to a

duty or responsibility of the design professional to the contractor, subcontractors, material and equipment suppliers or other persons or entities performing the work. Extremely cautious design professionals may modify the authority to reject work language so that the design professional merely has the authority to recommend that the Owner reject the work, and include an indemnity provision requiring the Owner to defend and indemnify the design professional for Owner decisions made against the design professional's advice.

Tips to keep in mind:

- Design Professional's obligation during construction phase is to "endeavor to guard the Client against defects and deficiencies"
- Site visits are for "observation" and not "inspection"
- Specify the number or frequency of site visits
- Do not perform continuous or exhaustive site observations
- Review of submittals is for limited purpose of checking for conformance with information given and design concept and not for determining accuracy of details (dimensions, quantities, installation, or performance)
- Design Professional is not responsible for construction means, methods, sequencing, techniques, etc.
- Design Professional is not responsible for jobsite safety programs
- Design Professional cannot, and should not, accept authority to stop work, but can reject or recommend rejection of work

Contingency Fund

As discussed in the "Big 6" provisions section, including appropriate standard of care language in the professional services agreement is critical in managing the client's expectations regarding the design professional's services. While a general contractor may provide a guarantee of perfection for its work, design professionals are not required to perform perfectly and are required only to perform in a manner consistent with the degree of skill and care ordinarily exercised by similarly situated design professionals (provided the design professional's contract does not include language elevating the professional standard of care). It is important to ensure the client understands the distinction between the general contractor's performance guarantee and the design professional's standard of care. Since the design professional is not required to perform perfectly, some amount of minor errors and omissions contained in the design professional's drawings and specifications is expected and the fact that there are errors and omissions does not necessarily mean that the design professional breached the standard of care.

Negotiating a contingency fund to address such errors and omissions is a valuable way to establish the client's responsibility to assume the financial risk of a percentage of the errors and omissions. We recommend contingency fund language such as the following:

> *"The Design Professional makes no warranty, express or implied, that its design is free of errors or omissions. The Client and Design Professional agree that certain increased costs and changes may be required and are anticipated due to omissions, errors or inconsistencies in the Design Professional's drawings and specifications. Therefore, the Client agrees to set aside a reserve in the amount of _____ percent (___ %) of the estimated cost as a contingency to be used, as necessary, to pay for any premium costs associated with changes. The Client agrees to make no claim against the Design Professional or its consultants in connection with any increased cost*

within this contingency amount. If costs due to changes resulting from design errors, omissions or inconsistencies exceed the contingency, then the Design Professional shall be responsible for premium costs incurred by the Client above that sum, but only to the extent caused by the Design Professional's negligent acts, errors or omissions. In no event shall the Design Professional be responsible for direct costs that the Client would have incurred in the construction contract regardless of the Design Professional's error or omission, nor shall the Design Professional be responsible for any costs that constitute betterment or upgrades to the Project."

This contingency fund language is valuable because it establishes that 1. the client is solely responsible for a specific designated percentage of costs associated with errors and omissions and 2. the design professional's liability for costs above the contingency fund is limited to the extent such costs are caused by the design professional's negligence.

Insurance

Additional insureds

Clients often draft convoluted and detailed insurance provisions requiring, among other things, the design professional name the client as an additional insured on its professional liability insurance policy. Clients may expect the design professional to name the client as an additional insured because they are used to general contractors being able to name them as additional insureds on their commercial general liability policies. This request is an indicator that the drafter of the agreement is inexperienced with the limitations of professional liability insurance. Clients have to be educated that industry standards preclude design professionals from naming additional insureds on their professional liability insurance policies.

Subrogation

Subrogation claims are essentially claims for reimbursement. In the design professional context, these types of claims are typically filed by insurance companies in an effort to recoup costs the insurance company has paid on covered losses incurred by its insured. Subrogation can be illustrated by the following scenario: An owner of a resort hotel files a claim with its insurance company for damages the hotel suffered due to water infiltration. The insurance company paid the insured's claim based on the covered loss and subsequently files a subrogation action against the design team and contractor seeking to recover the costs it paid to its insured. We recommend design professionals include mutual waiver of subrogation provisions in contracts with their clients, such as the following:

"The Client and Design Professional waive all rights against each other and against the contractors, consultants, agents and employees of the other for damages, but only to the extent covered by any property or other insurance. The Client and Design Professional shall each require similar waivers from their contractors, consultants and agents."

This type of mutual waiver of subrogation provision may benefit the design professional more than the client because subrogation actions tend to "skip" the owner-client level. Referring to our hotel example, note that the insurance company did not include the hotel owner as a party in its subrogation action. Rather, the insurance company excluded the owner and filed the subrogation action against the design professional team and contractor.

Tips to keep in mind:

- Design Professional cannot name additional insureds on workers compensation or professional liability insurance
- Professional liability insurance is per "claim" not "occurrence"
- Waiver of subrogation provisions should be mutual
- Delete requirement that professional liability insurer provide notice to Client if aggregate limit available for claims decreases or erodes
- Confirm design professional has coverage in place conforming to contractual insurance requirements

Peer Reviews

If a client undertakes a third-party or peer review for a project, we recommend negotiating language that outlines the client's and design professional's responsibilities with respect to the review. The client should bear all costs associated with the review and the design professional's schedule and compensation should be modified as reasonably required. The provision should also include broadly worded release and indemnity language in the event the design professional objects to the recommendations, but is nevertheless instructed by the client to modify its instruments of service. We recommend language such as the following:

> *"In the event the Client retains a third party ("Third Party") to conduct constructability or peer review(s) for the Project, it is understood that the Client shall pay all costs and expenses associated with such review(s) and that the review(s) shall be completed in a timely manner so that the performance of the Design Professional's services is not unreasonably delayed. The Design Professional shall not be liable for any delays arising out of or resulting from the Third Party review process, including time required to retain the Third Party, time required for the Third Party to conduct its review, and time required by the Design Professional to assess and respond to the Third Party recommendations. The Design Professional shall be compensated for the time required to assess and respond to the Third Party's recommendations. In the event that the Design Professional subsequently modifies its instruments of service as a result of the Third Party's recommendations, the Design Professional's schedule for performance and compensation shall be modified as reasonably required. The Design Professional shall have the opportunity to review and provide its professional opinion of the Third Party's recommendations. The Design Professional shall communicate any objections to the Third Party's recommendations, in writing to the Client, within 30 days of receipt of the Third Party's report for Client's evaluation and further consideration. In the event the Client requires the Design Professional to comply with the Third Party's recommendations despite the Design Professional's objections, the Client shall waive any and all claims against the Design Professional and release, defend, indemnify, save and hold the Design Professional harmless from and against all claims, losses, liabilities, demands, and damages arising out of or resulting from the incorporation of the design modifications required by the Client."*

Tips to keep in mind:

- Client should pay all costs associated with peer review
- Design Professional should not be liable for delay resulting from the review and Design Professional should be paid for time required to review and respond to recommendations

- Client should waive claims and indemnify Design Professional for damages arising from modifications if Design Professional objects to the third party's recommendations

Prototype Designs

Providing prototype designs is inherently risky for design professionals for many reasons, including the fact that: 1. the design professional may not be able to provide any input on the intent or interpretation of its designs since the design professional will probably not participate in the construction phase of projects that use the prototype designs; 2. any error in the designs will most likely affect each project for which the designs are utilized which could result in significant damages depending on the number of times the prototype designs are utilized and the severity of the error; 3. the design professional will not be able to adapt its design to local codes or the circumstances of the particular site for each project; and 4. the client may make unauthorized changes in the design professional's design and the design professional could be responsible for resulting damages, or at a minimum, required to defend itself if brought into a claim based on its modified designs.

If a design professional decides to provide prototype designs to a client, it is important to negotiate protections in the design professional's professional services agreement, including language limiting the design professional's liability, a provision requiring the client to waive claims against the design professional and indemnify the design professional for claims arising out of the design professional's services, and a mutual waiver of consequential damages provision.

Tips to keep in mind:

- Negotiate a limitation of liability provision
- Require Client to waive claims and indemnify Design Professional
- Include mutual waiver of consequential damages provision

Replacing Another Design Professional

Projects where a design professional takes over for another design professional on a project that is already in progress may involve significant risk and require careful contract negotiation. If you are replacing a design professional, your agreement should address your use of the prior design professional's instruments of service and state that you are entitled to rely upon the accuracy and completeness of information provided to you by the client without the need for independent verification. Your agreement should include a provision stating the client warrants that it is either the copyright owner of any information transmitted to you, or has permission from the copyright owner to transmit such information, for your use on the project. You should also insist on indemnity protection and language limiting your liability.

Tips to keep in mind:

- Include language stating Design Professional is entitled to rely on information provided by Client
- Require Client to warrant that it owns or has permission to provide documents for replacement Design Professional's use
- Negotiate a limitation of liability and indemnity provision in Design Professional's favor

Scope of Service

It is very important that the design professional's agreement include a sufficiently detailed and defined scope of services so the parties fully understand what each party will, and will not, do during the course of the project. While the factual scenario of claims between design professionals and their clients vary, the underlying reason of practically every claim is disappointed expectations by one of the parties. A well-drafted scope of services is a proactive way to manage the client's expectations and avoid disappointments with respect to what the client can anticipate from the design professional during the project. When addressing scope of services, the design professional should apply the acronym CDC, which stands for Clarity, Definition, Competency.

Clarity: The scope of services should be clear. The scope should not include ambiguous language and should consider the client's level of sophistication when outlining the services. Design professionals should make sure their scope of services is crystal clear if they are working with a less experienced client.

Definition: The scope of services should explicitly define the limits of the design professional's basic services. We discourage drafting a scope of services that only lists the services that the design professional will not perform because it is impossible to list everything that falls into that category. We recommend the scope clearly define, both by inclusion and exclusion (to the extent known), the services the design professional will provide. The scope should avoid "absolutes" and "unlimiteds" which produce an open-ended scope. Words such as "all"; "complete"; "each and every"; and "all necessary" are terms that are considered unacceptable.

Competency: The design professional should ensure that the scope falls within its traditional role and that it has the manpower and skill set to carry out the scope of services. If necessary, a design professional should consider using consultants for the project. A design professional that is a prime consultant should ensure consistency of its agreement with its consultant's agreements. Conversely, a design professional acting as a consultant should carefully review a prime agreement, preferably before it is executed.

Tips to keep in mind:

- Ensure scope is sufficiently detailed and defined
- Delete broad language requiring "any and all services necessary"; "complete design services"; and "adequate to meet the needs of the project"

Severability

A well drafted contract should address the concepts of severability and survival to ensure that the entire agreement will not be declared void by the court in the event a specific provision is deemed unenforceable or illegal. A severability provision provides that if a specific provision is illegal or unenforceable, the offending provision will be severed, or cut out, from the agreement. A survival provision ensures that in the event a provision is severed from the agreement, the remainder of the agreement remains in full force and effect as written. Since the severability and survival concepts benefit both parties, client-generated agreements very often contain appropriate language addressing these issues. An example of a severability provision is as follows:

"In the event any term or provision of this Agreement is found to be illegal or

otherwise unenforceable, the unenforceable provision will be stricken from the Agreement. Striking such a provision shall have no effect on the enforceability of the Agreement and the remaining terms and conditions shall continue in full force and effect as if the unenforceable provision were never included in the Agreement."

Tips to keep in mind:

- Include language so that unenforceable / illegal provision(s) will be stricken from agreement
- Clarify that striking provision(s) does not void the entire agreement, just the offending provision(s)

Third Party Beneficiaries

A third-party beneficiary is a party that is not a party to a contract, but who has legally enforceable rights under the contract. For example, if a professional services agreement between a design professional and its consultant includes a provision stating that the owner is an intended third-party beneficiary, the owner arguably has rights under the Design Professional / Consultant agreement, including causes of action for breach of contract and negligence seeking damages for economic loss, despite the fact that the owner is not a party to the agreement (or in legal parlance, is not in "contractual privity" with the design professional's consultant).

Third-party beneficiary status may be important when determining whether a consultant owes a duty to the owner since the concept of contractual privity generally stands for the proposition that contracting parties owe a duty of care to each other, not third parties with whom they have no contractual relationship. While jurisdictions vary in their interpretation of whether a design professional owes a duty of care to another party with whom the design professional has no contract, based in large part on the application of the economic loss doctrine, including contract language explicitly stating there are no third-party beneficiaries may help a consultant successfully argue to a court that a party with whom they have no contract and who is seeking economic damages has no standing to assert such a claim.

Based on the commentary above, we recommend design professionals include a contract provision expressly stating there are no intended third-party beneficiaries, such as the following:

> *"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. Design Professional's services hereunder are being performed solely for the benefit of the Client, and no other entity shall have any claim against the Design Professional because of this Agreement or the Design Professional's performance or nonperformance of services hereunder."*

Owners often request design professionals include language in their professional services agreement with the design professional's consultants stating the owner is an intended third-party beneficiary. In our example above, including such language in the Design Professional / Consultant agreement presents more potential exposure to the consultant than the design professional since the owner is already in contractual privity with the design professional and the intent of the third-party beneficiary language is to establish the owner's right to establish rights and assert claims against the consultant.

Tips to keep in mind:

- Delete any third-party beneficiaries
- Contract should explicitly disclaim any third party beneficiaries

Time Limit to Bring Claims (Statue of Limitations and Statue of Repose)

Statutes of limitations

Statutes of limitations are state statutes that establish the maximum time limits for a party to initiate a claim against another party. These statutes vary by state and by the type of action, but all statutes of limitations provide a "cut off" date after which a cause of action is time barred. If a claimant files suit beyond the applicable statute of limitations, the action is subject to dismissal. The critical issue when assessing a statute of limitations defense is establishing when the statute of limitations period began to run.

The general rule is that statutes of limitations begin to run upon accrual of the claim. However, many jurisdictions follow the "discovery rule" which provides that the statutes of limitations do not begin to run until the claimant discovers, or reasonably should have discovered, the harm that is the basis of the claim.

The AIA 1997 Owner / Architect agreements contained favorable language for design professionals, providing that the statutes of limitations began to run on the earlier of the date of substantial completion or the date of issuance of the final certificate of payment. This language helped design professionals because it fixed the date on which the statutes of limitations began to run at two easily identifiable and early dates. Of course, owners complained that the provision obviated applicable law and negated the discovery rule. In 2007, the AIA substantially modified the provision.

The 2007 provision addressing claims requires the parties to initiate dispute resolution proceedings within the time periods specified by applicable state laws, or within ten years of the date of substantial completion, whichever occurs first. Although the new language is not as favorable from the design professional's perspective, it is a reasonable compromise. The modification allows owners the benefit of the discovery rule in states that apply the rule, but it protects the design professional from exposure to potential liability beyond ten years after substantial completion.

Statutes of repose

Statutes of repose are state statutes that establish the maximum time limit for a party to initiate a claim against a design professional. They typically differ from statutes of limitations in two material respects. First, they run from a fixed point in time, generally the date of substantial completion or date of occupancy of the project. Unlike statutes of limitations, statutes of repose cannot be tolled and are, therefore, absolute time bars after which no claim can be initiated against a design professional. Second, the time frames are longer. While statutes of limitations for negligence claims typically range from two to four years, statutes of repose often range from six to twelve years.

Statutes of repose offer great protection to design professionals, who otherwise would face potentially endless exposure from a temporal standpoint. Not every state has a statute of repose, and the types of claims to which they apply and the

timeframes can vary greatly from state to state.

Tips to keep in mind:

- Establish specific point in time when statute of limitations begins to run (ex: date of Substantial Completion)
- Delete references to the discovery rule ("discovery of the harm complained of")
- Delete language unreasonably limiting design professional's time to assert claims
- Delete any "under seal" language in signature blocks since this language significantly extends applicable statute of limitations and repose in many states

Timeliness of Performance

We recommend design professionals delete "time is of the essence" statements. Clients often include this sentence in the schedule provision of the agreement to emphasize the importance of the client's proposed schedule. This sentence is problematic because it implies that the design professional guarantees it will comply with the client's schedule regardless of any intervening factors. If the design professional is unable to delete this sentence in its entirety, we recommend the design professional add a sentence stating that the client recognizes that the design professional's performance must be governed by sound professional practices. This qualifying language provides the design professional with some protection and negates the implied warranty by tying the design professional's responsibility to comply with the schedule to the applicable standard of care. However, this contracting tactic requires the design professional to ensure the standard of care provision does not contain warranty language and is appropriately negligence-based.

Tips to keep in mind:

- Design professional should perform "as expeditiously as is consistent with the professional standard of care"
- Delete "time is of the essence" provisions
- Time limits established by agreed upon schedule can be exceeded under reasonable circumstances
- Delete any liquidated damages provisions for failure to meet schedule
- Allow for delay due to force majeure events
- Design Professional only responsible for delay costs to the extent those delays costs are caused by the Design Professional's negligence

Waiver of Consequential Damages

Consequential damages are those damages that are not direct. The potential for substantial consequential damages is particularly acute on projects that rely heavily on the stream of commerce and profits, such as casinos, shopping malls, hotels, and restaurants. It is not unusual for clients to assert significant consequential damages claims in connection with those types of projects, often originating from delays in opening dates. We recommend including a mutual waiver of consequential damages provision whereby both the design professional and client waive their rights to seek incidental, indirect, and consequential damages, especially when providing services on projects that rely on the stream of commerce. An example of a mutual waiver of consequential damages is as follows:

> *"Neither the Client nor the Design Professional shall be liable to the other or shall make any claim for any incidental, indirect or consequential damages*

arising out of, or connected in any way to the Project or this Agreement. This mutual waiver includes, but is not limited to, damages related to loss of use, loss of profits, loss of income, loss of reputation, unrealized savings or diminution of property value and shall apply to any cause of action including negligence, strict liability, breach of contract and breach of warranty."

Tips to keep in mind:

- Particularly important in projects relying heavily on stream of commerce (casinos, shopping malls, restaurants, hotels, etc.)
- Waiver should be mutual

Conclusion

The importance of negotiating an appropriate professional services contract cannot be overstated. A well-drafted contract will detail the rights and responsibilities of the parties and may provide valuable protections to the design professional in the event of a claim. As a broker, design professionals may turn to you for help drafting and negotiating their contracts. This document highlights provisions commonly found in professional services contracts from a risk management and professional liability perspective. However, each project, and therefore each contract, presents unique risks and challenges that should be addressed from a business, legal and risk management perspective and there could be specific issues under the applicable law governing interpretation and enforcement of the contract for which the design professional should seek the assistance of a local attorney.

For more risk management information, please visit Beazley's A&E Risk Management Website at **www.beazley.com/A&E** or contact **colleen.palmer@beazley.com**.

The information set forth is intended as general risk management information and should not be construed or relied upon as legal advice. It is not intended as a substitute for consultation with counsel. There could be specific issues under the applicable law for which you may want to seek the assistance of a local attorney.