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Indemnities, Part 1: Avoiding Added and Uninsurable Liabilities

A Time for Transitional Leadership

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No question. Things are changing, and changing fast. Few like change;

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Start Your Benefits Renewal Process Now!

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Is your benefit program due to renew in January? Think you can wait until fall to start the renewal process? It's best not to—give yourself time to evaluate your options and select the best fit for the best price.

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By Doris Livingston
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(See page 2 for insurance & risk management tips)



When times get tough, more and more design firms are competing for fewer and fewer projects. In such an environment, some project owners are more apt to put the squeeze on architectural and engineering firms. Not only are project fees cut to the core, but these clients are apt to ask for more onerous contract conditions – and design firms are more willing to accept them when jobs are scarce. Indemnity clauses, in particular, are showing up more often among the list of client demands.

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Indemnities

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Indemnity agreements between design firms and their clients present a minefield of liability risks and legal troubles. By agreeing to a client's onerous indemnity agreement, your design firm may be saddled with virtually all project risks – with many of the liabilities uninsured. That's why it is imperative for you to understand the issues surrounding indemnities and to work with your attorney to ensure that your client agreements do not put you in an untenable position.

Why Indemnity Agreements?

The concept of indemnification originated in the construction industry as a method to hold project owners harmless from liabilities that arise during construction. The basic concept makes sense: since the contractor has control of the jobsite, it should indemnify – or hold harmless – the project owner for any site-related liabilities that arise. If a worker or visitor is injured on a construction site, for example, the contractor is held responsible since it controls jobsite safety.

Over time, the concept of indemnification has been altered in ways that are unfair to design consultants. Architects and engineers are often asked to sign indemnity agreements that make them assume a large portion of project risks. Indeed, it is not uncommon for design firms to find one or more contract clauses requiring them to indemnify the client from substantial liabilities, including those over which the designer exercises no control. The indemnification language may be short and seemingly innocent, or lengthy and complex, but it spells serious trouble either way.

Many design professionals concede that they have unwittingly encouraged clients to use onerous indemnifications by accepting them so readily. If they balk at an indemnity, the client may say, "Well, XYZ design firm down the street doesn't object to the language." Fearing they might lose the job, the design firm disregards better

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Insurance & Risk Management Tips

Reduce Your Social Host Liquor Liability Exposure

The [National Highway Traffic Safety Administration](#) estimates that nearly 13,000 people per year (about 35 per day) are killed in alcohol-impaired driving crashes.

Many of these tragic accidents happen after an inebriated person leaves a party – an event in which the host of that party might be held liable for injuries and deaths to innocent parties. Although there might be coverage under your personal auto policy or homeowners policy if you (as the host) are held legally responsible for such a terrible accident, a wiser risk management strategy is to avoid or reduce the chance of loss altogether. With that in mind, here are some tips to consider if you (or a resident family member) occasionally host social events involving alcohol.

- Surveys of youth indicate that the most common source of alcohol is the young person's own home. Thus, closely monitor social events your youth hosts to make sure there is no drinking allowed -- particularly any

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Types of Client-Drafted Indemnities

Client-drafted indemnities used in the design & construction industry can be separated into three types.

Broad unilateral indemnities create the greatest problems. Such indemnities can make a design firm responsible for almost any problem that befalls its client during the project, whether or not the designer was negligent. A typical broad-form indemnity requires the consultant to agree to hold the client harmless for any and all liabilities, including defense costs, arising out of the performance of services. Note that broad-form indemnities do not limit the indemnification to liability that is the result of the design professional's negligent acts, errors or omissions. Obviously, such an all-encompassing indemnification creates enormous and largely uninsurable liabilities.

In some states, broad-form indemnification has been made illegal by virtue of court decisions or anti-indemnification statutes passed by lawmakers. But even in states where such broad indemnities are illegal, a judge might still rule that a given clause will be enforced when the parties to the contract have enjoyed relatively equal bargaining power and the clause is written so clearly that its intent is unmistakable.

Unilateral negligence indemnities are not much better than broad-based ones, but they are more likely to be held as legal in many jurisdictions. These indemnities provide that a design professional will cover all of the client's risk whenever the design professional shares some liability due to negligence. A typical unilateral negligence indemnity requires the design firm to agree to hold harmless and indemnify the client from any and all liability, including cost of defense, arising out of the consultant's negligence, whether it be sole or in concert with others, in connection with performance of contracted services.

Given a clause such as this, the client could be 99% at fault, but as long as the designer is at least 1% at fault, the consultant picks up 100% of the tab. And in the event of a project upset, there is a very high likelihood that a design consultant would be held partly at fault. In fact, virtually any attorney could convince a jury that a design professional had at least a minor role in a project upset.

Proportionate-negligence indemnities assign liability to the parties involved in proportion to the degree of fault. For example, if you are found to be 20% at fault, you will pay 20% of the damages. With a typical proportionate-negligence indemnification, the consultant agrees to hold harmless and indemnify the client from and against liability arising out of the consultant's negligent performance of services. Damages, however, are shared with the client, contractor and other parties on a proportionate-fault basis as determined by a mediator, arbitrator, judge or jury.

While this limited indemnity is certainly more acceptable than the other two, it is best not to have it in a contract. First, it is unnecessary since you are already liable for your negligence. Second, it could muddy the waters regarding the insurability of your errors and omissions.

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Indemnities

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judgment and signs an indemnity-laden contract.

But before signing on that dotted line, consider:

- Client-drafted indemnities ask you to assume liability for others' negligence. Ask yourself: without the indemnity, whose risk would it be? Almost invariably it would be the client's or contractor's risk.
- Most client-drafted indemnities are uninsurable. If you sign an indemnity agreement, more likely than not you are accepting liability beyond that required by law or the prevailing standard of care. Your professional liability policy likely specifies that the insurance does not cover any liability you assume voluntarily by contract unless you would have been liable in the absence of the contract.
- Client-drafted indemnities frequently contain unclear language that can be broadly interpreted – and misinterpreted. For instance, a client may ask for indemnity for your "intentional acts." A crafty attorney could interpret virtually any of your acts as "intentional."
- Indemnity agreements may require you to pay for the client's legal defense in the event of a claim or lawsuit. This provision could be interpreted as an obligation on your part to retain an attorney for your client and pay for this defense – even if no negligence has been established. In some states, these legal costs are not considered recoverable damages and therefore may not be covered by your professional liability insurance.
- Client-drafted indemnities may include inappropriate parties to be indemnified. You should never agree to indemnify a client's agent, contractor, attorney, contract employee, lender, vol-

unteer or anyone else who is not directly part of the client entity.

Making Your Stand

Regardless of how attractive a potential project may be, your guiding principle should be that you will not accept a client-written indemnity agreement. You must insist that liabilities remain with those parties who are in the best position to control them. You should do your best to persuade the client to remove any indemnity language that may increase your liability beyond that you already have for your negligence, errors and omissions. Specifically, be sure you:

Know the law. Working with your attorney, find out whether your state or jurisdiction has anti-indemnification statutes on the books. If so, what do they say and how have the courts interpreted them? Be aware that the law in your state may not apply to your project disputes. Client-drafted contracts frequently require that disputes be settled in the jurisdiction where the client is located and/or where the work is performed. This may be an out-of-state location where indemnities are enforceable.

Educate your client. Perhaps the best tactic for getting rid of an unfair indemnity is to demonstrate to the owner the ineffectiveness of such a contractual stipulation. Point out any anti-indemnification statutes on the books in your state or the jurisdiction.

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tion where any dispute would be tried. Explain that any indemnification that expands your liabilities will be uninsurable and could even jeopardize coverages that would apply without the indemnification. As your insurance agent, we can help explain to your client that you are already liable for your errors and omissions and any resulting damages are covered within the available limits of your professional liability insurance policy. We'll explain that an indemnity is unnecessary and may cloud the issue of your insurance coverage and legal responsibilities.

Plead for fairness. Explain that to hold you legally responsible for another's liability is simply unfair. Reaffirm your willingness to accept responsibility for your own errors and omissions but state your unwillingness to be liable for the mistakes and oversights of others. Explain that the theory of indemnities applies to contractors on the construction site since they assume control over the work site. Make clear that you don't exercise that control and that it is unfair to hold a design firm responsible for liabilities that are completely out of its control.

Convincing an owner that an indemnification would be unenforceable and/or unfair can be difficult when the client has paid an attorney to draft the contract and the client has been told that another design firm will agree to the provision. What do you do when a plea for basic fairness does not work? There are still some options that while not ideal, are far better than accepting a client-drafted indemnity.

Next issue, Part 2 of this two-part report will address those alternatives. Plus we will examine certain cases where you might want to request indemnities from a client.

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

Liquor Liability

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type of illegal underage drinking.

- Limit the amount of alcohol at your event.
- If alcohol is served at your party, make sure that there is plenty of food. The consumption of food slows down the absorption of alcohol.
- Encourage designated drivers and provide nonalcoholic drinks for these guests.
- Look for signs of intoxication. Restrict alcohol to any near-intoxicated or intoxicated persons by offering instead some food or alternative nonalcoholic drinks.
- Consider hiring trained bartenders. As they are trained to recognize and deal with intoxication, using professional bartenders can significantly reduce the risk and may help in defending a claim should there be one.
- If you have a cash bar, use tickets and issue a limited number. Don't price alcohol too low because this encourages excessive drinking.
- Do not allow the intoxicated guest to drive away from the event even if you have to take away his or her car keys. Instead, offer to drive them

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Transitional Leaders

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many resist change. Right now, with or without you, change is happening all around.

It's hard to find positive in the type of negative change we've been experiencing, but it's starting. We are moving through stages of dealing with the outside environment, and I really like what I am starting to see happen right now.

Last fall, we experienced a new form of shock and awe as the bottom seemed to fall out of everything. Our businesses were hit by the impact at different points, depending on our client base and project backlog, but now we all understand how the A/E industry has been affected.

Then it seemed like everyone moved into a holding pattern. Maybe it was winter; maybe it was a bit of disbelief that this really would last beyond 2Q 09, but things kind of stood still, waiting.

But now something else is happening. I am seeing our leaders looking out, defining a preferred future, and putting steps in place to get there. This is the heart of transitional leadership.

For many years, many of us have been operating at +100%, dealing with the hottest fires and cranking out deliverables to meet never-ending deadlines. Few, if any of us, are at 100% capacity right now. And while the leadership in many firms has their back against a wall to keep firm doors open, leaders are starting to move beyond damage control and look to the future:

- What should the firm be in five years?

- How should our business model change?
- What expertise should our staff have?
- What clients should we be serving?

Leaders have time to give deserved thought to, and take action on, business strategies that have been begging for attention for years.

Fast Company ran an article in the July/August 2009 issue called Create Your Own Economy. It talked about changing how we measure growth in our firms. While I can't say that I agreed with all of the points in the article, it touches on a concept that I continue to think about: the traditional gauge of economic success is profit, but profit doesn't tell us much about broader efforts to improve human well-being. I would argue that profit also doesn't tell us much about broader efforts to improve our business's well-being.

Given the inevitable impact of global influences, the lightening speed of technological advancements and the economic shake up that has thrown us from our areas of comfort, I believe we are entering into a period of transitional leadership that we have not experienced before.

A colleague of mine described it this way: "it's like we are recovering from an economic stroke, and our neurons are looking for new pathways to get things back on their feet." Leaders in our industry are networking and exploring ideas that they haven't had the time or need to explore before.

We may not post record profits this year, but maybe we'll accomplish much more.

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