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CALIFORNIA DESIGN PROFESSIONALS: INDEMNITY & DEFENSE/ THE WORLD AFTER *UDC V. CH2M HILL*

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In January, the California Court of Appeals issued a decision which dramatically expands the historical exposure of design professionals under relatively common indemnity and defense provisions in professional service Agreements. Specifically, the case was *UDC-Universal Development, L.P., v. CH2M Hill* (DAR January 15, 2010). Efforts to have the decision reviewed by the Supreme Court have been rejected. Accordingly, this decision will go forward as the most current statement of design professional indemnity and defense obligations and exposures in California. That reality is, and should be, of great concern to California design professionals and their insurance carriers. It compels more vigilance and scrutiny than ever with respect to drafting, negotiating, and agreeing to indemnity and defense clauses.

In this Appellate decision, the Court held that even though design professional CH2M Hill successfully defended itself and defeated the underlying claims of negligence, CH2M Hill was still obligated to reimburse its client, the developer, for attorneys' fees and costs incurred in the action. The decision has drawn significant industry attention because the indemnity language was ostensibly limited "to the extent" of CH2M Hill's "negligent act or omission". Historically, this has been believed to be an appropriate model for design professionals to follow. The point of this discussion is two-fold:

1. For Agreements currently under negotiation, what can design professionals better their position to avoid the fate suffered by CH2M Hill? and
2. Where such Agreements are already in existence, what can design professionals and their insurance carriers do to manage and mitigate the financial risk?

Contract Drafting & Negotiation

For purposes of present and future contract negotiations, there are at least three obvious steps design professionals can take to differentiate their position from that of CH2M Hill. The specific contract language controlling CH2M Hill's obligations was as follows:

"Consultant [CH2M Hill] shall indemnify and hold Owner, Developer, and their respective officers, directors, employees and agents free and harmless from and against any and all claims, liens, demands, damages, injuries, liabilities, losses and expenses of any kind, including reasonable fees of attorneys, accountants, appraisers and expert witnesses, to the extent they *arise out of or are in any way connected* with any negligent act or omission by Consultant, its agents, employees or guests, whether such claims, liens, demands, damages, losses or expenses are based upon a contract, or for personal injury, death or property damage *or upon any other legal or equitable theory whatsoever*. Consultant agrees, at his own expense and upon written request by Developer or Owner of the Subject Property, to defend any suit, action or demand brought against Developer or Owner on any claim or demand covered herein. Notwithstanding the above, Consultant shall not be required to indemnify Developer or Owner from loss or liability to the extent such loss or liability arises from the gross negligence or willful misconduct by Developer, Owner, or agents, servants or independent contractors who are directly responsible to Developer or Owner, or for defects in design furnished by such person." (Italics added.)

Design professionals can improve on this language, as follows:

1. Separation of the defense obligation into a separate sentence was clearly a factor in this decision. As discussed below, that can be a good strategy. However, as drafted here, it was arguably a more expansive obligation than the preceding indemnity language and not clearly limited by the "to the extent" language. The defense obligation should now be limited to actual negligence if set forth separately or as part of the indemnity language.
2. The catchall closure of the indemnity sentence was also a contributing factor. The words "or upon any other legal or equitable theory whatsoever" influenced the Court to see the obligation as broader and more expansive than it might have been otherwise. Such catchalls should be avoided whenever possible since they can lead to unpredictable consequences.
3. Similarly, the language which referenced claims which "arise out of or are in any way connected with any negligent act or omission" was overbroad and expansive. It would have been far better to limit the obligation to claims "caused by the negligent act or omission". Causation is a legally-recognizable and confined term which ties acts to consequences.
4. Finally, following this decision (as well as its predecessor *Crawford v. Weather Shield Mfg. Inc.*), it is imperative that the limitations be even more specific than historically required. The provision must now more emphatically limit the obligations to those solely attributable to actual negligence. There are many ways to do this. It can be by a separate defense clause requiring proof of actual negligence to trigger the obligation. Alternatively, it could be part of the serial indemnity provision, but limited by the word "solely" to avoid any judicial

implication that any of the obligations extend beyond the proportionate responsibility based on actual negligence.

Following the *UDC v. CH2M Hill* decision, design professionals have a number of options for strategic contract drafting and negotiation. In strategic order of value, they are as follows:

1. Simply strike any indemnity and defense clause. The basis for this can be that it is an uninsured exposure as well as referencing the unpredictable interpretations and all applications from the Courts.
2. If any indemnity or defense obligation is a necessary reality, make clear that it is limited to actual negligence or breach of duty. It may no longer be sufficient to simply say "to the extent caused by . . .". It may now be necessary to negate any statutory or judicial implication by a negative declaration. Such a phrase might read:

"Any indemnity or defense obligation shall be limited to Consultant's actual and proportionate negligence or breach of duty."
3. If such negative declarations are not accepted, making the indemnity and defense obligation mutual can blunt many of the impacts because it would create complete and potentially-canceling claims.
4. Another option, and one potentially even more valuable to the long-term relationship, would be to establish a joint defense model in the Agreement whereby each party would defend issues alleged to be its responsibility for the benefit of both parties. This fosters an allegiance between the design professional and its client, and limits the expenses of defense by assigning issues to the party best able to respond.
5. Finally, if all of the preceding are unavailing, the design professional could limit the obligation to a dollar figure or to available insurance coverage. The latter may be the best subtle defense in that there may seldom be insurance coverage for such claims.

Existing Contract Language

Many design professionals will inevitably have existing Agreements (and even future Agreements) which will risk the same judicial interpretation as that received by CH2M Hill. Rather than simply accepting that fate, there are at least two responses which may eliminate or dramatically reduce the financial exposure and risk:

1. **Joint Defense.** By definition, such indemnity claims arise only where the client has received a claim from a third party, and then looks to the design professional to respond to that claim. Often, such claims become significantly worse where the client and design professional engaged their separate litigation teams and pursue the battle with intensity and accompanying finger-pointing. Not only is such a battle expensive, but it also most often inures to the benefit of the third-party claimant who can just sit back and benefit from the evidence and claims developed by others. A Joint Defense Agreement is a litigation Agreement which allows for a united defense, sharing of information, and related sharing of some costs. Such an arrangement may even be negotiated at the outset as part of the professional service Agreement, as a means of administering the indemnity and defense obligation.

2. **Issue Defense.** Absent a Joint Defense Agreement, a design professional faced with potentially-unfavorable defense and indemnity obligation may greatly blunt the defense expense exposure by agreeing to assume the lead defense of the relevant design allegation and assuring the client that it may rely on and benefit from that defense. When issued in a written affirmation, this may undermine any future claim that the client had to expend any of its defense dollars in defense of the design issues. Typically, a client would have its own issues to defend which would in turn be responsible for its own defense costs.

Each of the foregoing solutions is a delicate dance and should be developed in close consultation with both insurance carriers and legal counsel.

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² *Severson & Werson has provided legal services throughout California and the country for more than fifty years. The firm provides counseling and litigation support to all members of the construction process, including design professionals, construction managers, environmental professionals, owners, contractors, and insurance carriers.*