



The Indemnity Dilemma

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The most frequent and frustrating kinds of claims against design professionals arise out of construction site accidents. It is well established that the contractor, not the architect/engineer, is responsible for jobsite safety. Yet, whenever a workman is injured, it is a good bet that the A/E will be sued along with the contractor and any other potentially involved parties.

In these cases, the design professional usually prevails, but only after having spent thousands of dollars in attorney's fees, all chargeable to the A/E under the deductible in the professional liability insurance policy. Meanwhile, the contractor (and usually the owner), is defended under a general liability policy with a small or non-existent deductible, so that the lawsuit ends up costing them virtually nothing except some time and bother.

Sophisticated design professionals employ several contractual devices to attempt to limit their liability in these situations. The three most frequently used devices are:

1. Limitation of liability clauses
2. Indemnity clauses
3. Being named as an additional insured on the contractor's insurance policy.

Limitation of Liability Clauses

These are clauses that state that the design professional shall never be liable for more than a given sum as a result of any error or omission committed by the design professional. The sum chosen may be the limit of the A/E's insurance coverage, the total fee received by the A/E for the project, or any other randomly chosen number.

The problem with these clauses is that they solve the wrong problem. Although the courts have held them to be enforceable, they are only effective against the other party to the contract, namely the owner. An injured workman, who has not signed any agreement limiting the A/E's liability, will not be bound by the limitation of liability clause.

Indemnity Clauses

Indemnity clauses seek to make the contractor responsible for both assuming the A/E's defense and making any necessary payment of settlement or judgment in a worker injury case. This clause must appear in the Owner/Contractor Agreement to be effective against the contractor. In the AIA A201 General Conditions document, the indemnity clause is found in Section 3.18. Most of the standard form construction agreements contain essentially similar indemnity clauses.

All of the standard form indemnity clauses contain various flaws or weaknesses. Since they are in the *Owner/Contractor Agreement*, they can be modified or deleted without the A/E's consent. This can be remedied by including a provision in the A/E Agreement requiring the owner to include the intact indemnity clause in the construction contract. Most indemnity clauses do not include reimbursement of the design professional's costs and attorney's fees spent enforcing a recalcitrant contractor to abide by the terms of the clause. They do not include a waiver of the contractor's right to contribution, and they do not explicitly make the A/E a third party beneficiary.

These flaws are relatively minor and easily correctable. In Illinois there is a far worse flaw. Under the Illinois Anti-Indemnity Act (Ill. Rev. Stat. ch. 29, section 61), these indemnity clauses are rendered either entirely void or largely useless.

The Illinois Anti-Indemnity Act states:

"With respect to contracts or agreements, either public or private, for the construction, alteration, repair or maintenance of a building, structure, highway bridge, viaducts or other work dealing with construction, or for any moving, demolition or excavation connected therewith, every covenant, promise or agreement to indemnify or hold harmless another person from that person's own negligence is void as against public policy and wholly unenforceable."

This law has been held applicable to claims for violation of the Illinois Structural Work Act as well as to claims of pure negligence.

At least in practice, the Anti-Indemnity Act renders indemnity clauses little more than useless. Whenever an injured worker sues an A/E, the complaint is going to allege negligence or a violation of the Structural Work Act. When the A/E demands that the contractor indemnify it, the contractor will refuse, claiming the indemnity clause to be void since it requires indemnification against a claim of negligence. Then the design professional is forced to defend himself or herself.

Under this law, the only value of an indemnity clause is when the A/E successfully defends himself or herself and obtains the court's finding that the A/E was not negligent. Then, only after incurring all of the defense costs, can the A/E attempt to seek reimbursement from the contractor. And even this remedy is uncertain and expensive, since the contractor would likely claim that the Anti-Indemnity Act

renders the entire clause void, regardless of the A/E's successful result in court.

An important loophole in the Anti-Indemnity Act is that it does not apply to contractual provisions that require a contractor to purchase insurance covering another party's negligence. These provisions are still valid and enforceable. However, the insurance industry has its own pitfalls.

The A/E as an Additional Named Insured

When preparing the insurance provisions of the specifications, the savvy A/E includes a requirement that the contractor name the design professional as an additional named insured on the contractor's liability policies. The theory is that when the contractor's general liability insurer defends a jobsite accident claim on behalf of the contractor, the insurer can simultaneously defend the design professional. The effect would be the same as an indemnity clause: the insurer pays the attorney's fees to defend the claim, plus any settlement payment or judgment, up to the limit of the policy.

There are two problems with this risk-shifting device — one minor and one major. The minor problem is that contractors' general liability carriers often refuse to name the A/E as an additional insured unless professional liability insurance is also carried by the A/E. The major problem is that contractors' general liability policies do not cover negligence claims against design professionals.

In the eyes of the law, an A/E has a different status from a contractor or owner. The A/E is a professional, held to a different standard of care. A negligence claim against a contractor (or owner) is considered a general liability claim, but a negligence claim against a design professional is considered a professional liability claim.

Contractor's general liability policies all specifically exclude coverage for professional liability claims. The courts have upheld this distinction. Thus, even if essentially identical negligence claims are made against an A/E and a contractor, the contractor's general liability insurer may properly defend the contractor (and owner) but refuse coverage of the design professional. Since virtually every conceivable negligence claim against an A/E will be a professional liability claim, being named as an additional insured on the contractor's general liability policy is next to useless.

A Possible Solution

Between the Anti-Indemnity Act and the coverage limitations in the insurance industry, it is virtually impossible to draft an effective risk-shifting clause in Illinois. The only potentially workable solution would be to require the contractor to provide professional liability insurance coverage for the design professional, with no deductible and at the contractor's expense. Although it has never been tested in the courts, the following clause attempts to shift the risks in a legal and enforceable manner:

Contractor promises and warrants that insurance coverage will be provided by the Contractor for the Architect, the Architect's employees, agents, and representatives, with insurance coverage defending and indemnifying them from any claims for bodily injury, death or property damage arising out of construction of the project, whether such claims are based on allegations of ordinary negligence, professional negligence, or violations of the Illinois Structural Work Act. This insurance coverage shall have a limit of \$_____ per claim with no deductible. All of the parties to the Project acknowledge that this insurance is probably not available on ordinary commercial markets and may be extremely difficult to obtain; however, Contractor shall not assert difficulty obtaining the insurance as an excuse for failure to obtain it. Architect hereby agrees that the sole remedy for Contractor's failure to obtain this insurance shall be to require Contractor to pay all damages incurred by Architect, the Architect's employees, agents and representatives arising out of such a claim because of the absence of the insurance: namely, all defense costs and attorney's fees, plus any indemnity or settlement payment. Architect is an intended third party beneficiary of this provision and shall be entitled to recover all costs and expenses, including attorney's fees, incurred in enforcing the terms of this provision.

This clause comes with no guarantees — a court might hold it to be an unenforceable attempt to circumvent the Anti-Indemnity Act. But there is no other risk-shifting clause currently in use in Illinois that stands a greater chance of success.

Conclusion

The indemnity dilemma illustrates the state legislature's failure to understand the problems plaguing the design industry. The Anti-Indemnity Act makes sense for construction contractors, who have a duty to provide safe working conditions. But it should not apply to design professionals who neither have a duty to ensure safety on the jobsite nor can take advantage of no/low deductible insurance policies.

About the Author

Mark C. Friedlander is a partner in the Construction Law Group at the law firm of Schiff Hardin LLP. He obtained his B.A. from the University of Michigan in 1978 and his J.D. from Harvard Law School in 1981. He is currently an adjunct professor at the University of Illinois at Chicago School of Architecture and a lecturer at Northwestern University's Engineering School, and had lectured at the Illinois Institute of Technology School of Civil Engineering from 1987-89, at the Engineering School of the University of Wisconsin in 1988 and 1990, and the Architecture School of the Georgia Institute of Technology in 1997-98. Mr. Friedlander concentrates his practice in construction law and litigation with particular emphasis on design-build methods of project delivery.

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