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Position Paper

Indemnities

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About this Paper

Note: This is an update to the paper released in June 2010.

An indemnity clause is a contractual provision that can operate to extend a consultant's liability beyond the scope generally recognized by law and beyond the scope of professional liability insurance coverage.

Indemnity provisions are a common source of dispute during contract negotiations between consultants and clients, often due to a lack of understanding of their legal implications. Clients, particularly large project owners, will typically seek to have consultants provide a contractual indemnity similar in nature to the indemnities given by contractors. Contractors, however, are in a much different position from consulting engineers on a construction project.

How indemnities differ for Contractors:

Contractors assume control of an owner's property and occupy it for the purpose of constructing the project. It is often therefore reasonable for the owner to ask the contractor to indemnify the owner for all damage or injury that arises on the site. The same logic does not apply to consultants. Consultants may have some site presence, but do not occupy or exercise control over the site in the manner contractors do. Consultants also do not control the Contractor's or Owner's workers nor the way the work is carried out.

Consultants engaged in construction projects should not accept indemnity clauses which cause them to assume liability greater than what would otherwise be imposed by law. Such indemnities are also unsuitable for consultants on non-construction projects.

Typical language:

Indemnity clauses in a contract often use terms such as:

> *"The Consultant shall defend, indemnify and hold harmless…"*
>
> *"The Consultant assumes the responsibility and liability for…"*

Clauses such as these should be reviewed carefully to assess the potential for unnecessary expansion of the consultant's exposure to liability. It is common to encounter several indemnity clauses in one client agreement. There is often a general indemnity clause as well as additional clauses specifically related to topics such as confidentiality, intellectual property, health and safety, and so on.

Scope of Liability

In addition to liability at law for breaches of contract, statutory requirements, and ethics, engineers and other professionals can be found liable in negligence. Negligence is established when four elements are met:

1) The professional must have a duty of care to the plaintiff (typically the client, but this could apply to others as well).
2) The professional must breach the duty of care.
3) The breach must be the cause of harm or damages – i.e., the harm or damages must be reasonably foreseeable because of the breach.
4) The client or other plaintiff must have suffered actual harm or damages due to the breach.

How indemnities expand liability:

Many indemnity provisions seek to expand liability beyond that for which a consultant would typically be liable. For example, client agreements reviewed by ACEC-BC sometimes include indemnity provisions with language like:

> *"The Consultant hereby assumes the entire responsibility and liability for all damage and injury of any kind and nature whatsoever, caused by, resulting from, arising out of, incidental to, or accruing in connection with the Contract or the Services…"*

A consultant who agrees to such language does so at significant risk:

- Such a clause has no limits on the type of damages recoverable (the damages need not be foreseeable, expected or anticipated by the parties at the time the contract was entered into and could include consequential losses and liquidated damages for which a consultant may not otherwise be liable).
- The liability falls upon the consultant without a need to establish negligence or fault.
- The language requires the consultant to indemnify the client for losses arising from a wide range of situations, including those beyond the consultant's control or expertise, and including losses that are not directly caused or contributed to by the consultant. Even remote or tangential connection to damage or injury results in liability!
- The consultant has assumed broad responsibility for the client's losses, well beyond typical liability incurred by consultants. For example, the language exposes the consultant to liability for third party claims (for which they may not otherwise be liable) since these could be among losses "of any kind and nature whatsoever". The consultant may also be exposed to joint and several liability – meaning the consultant can be liable for the full extent of the client's losses even if other parties are responsible, or to be fully responsible for the loss unless the client is solely responsible, thanks to the wording "entire responsibility and liability".

Indemnitees

It is important to carefully consider the *indemnitees* (parties to be indemnified) in relation to indemnity provisions. The parties may be specified within a list of definitions (i.e., via the client's name or a term such as "Indemnified Parties") and some of the listed parties may be inappropriate for a consultant to indemnify.

It is typically acceptable for a consultant to indemnify a client's partners, directors, principals, officers and/or employees, and in some cases related entities. A consultant should resist indemnifying parties not directly part of the client entity, such as agents, contractors, other consultants, attorneys, contract employees, lenders, volunteers or assigns (see Other Considerations for additional context).

Insurability of Liability

Perhaps most significant for many consultants, the liability assumed under an indemnity may not be insurable. Most, if not all, professional liability insurance policies *specifically exclude coverage for claims arising from liability assumed by the insured under contract*, including for breaches of contract and hold harmless or indemnity clauses (unless liability would have resulted without the indemnity). It is therefore important that consultants seek advice from an insurance broker, insurer, or lawyer regarding potential uninsured exposure prior to agreeing to any indemnity clause.

Provision to "Defend"

Client-drafted indemnities often include language requiring a consultant to "defend" the client. The most concerning aspects of this obligation are:

- The requirement to defend the client implies "up-front" defense, i.e., there is no requirement for the consultant's liability to be adjudicated before funding the defense. The consultant essentially shields the client from the claim without an impartial assessment of liability.
- Professional liability insurance policies will generally not cover the cost of such defense of a client because this obligation would not exist at law, i.e., the obligation only exists because the consultant accepted the indemnity clause.
- Broad indemnities with defense provisions can leave a consultant open to defending the client against claims that are unfounded and/or unrelated to the consultant's services.

Consultants should pay attention to developments in indemnity interpretation by the courts. For example, in Ontario, "hold harmless" has been interpreted by the courts to mean defending the client up-front[1]. Such interpretation could follow in British Columbia.

[1] Stewart Title Guarantee Company v. Zeppieri, (2009) O.J. No. 332

Putting it all Together

The order of preference for indemnification in a typical client-consultant agreement is:

1) No indemnification.
2) Mutual indemnification of each party by the other.
3) One-way indemnification of the client by the consultant, limited to the extent of the consultant's negligence.

The Canadian Construction Documents Committee Service Contract between Owner and Consultant 2020 (CCDC 31)[2], GC 6.2 includes an acceptable mutual indemnification clause, in addition to a limitation of liability. The mutual indemnification clause is as follows:

> *"Subject to the limitations of liability set out in the Contract, each party shall indemnify the other party, to the extent of the fault or negligence of the indemnifying party, for damages and costs resulting from:*
>
> > *.1 a breach of contractual obligations under the Contract by the indemnifying party or anyone for whom that party is responsible; or*
> >
> > *.2 negligent or faulty acts or omissions of the indemnifying party or anyone for whom that party is responsible."*

A standard one-way indemnification clause developed by ACEC-BC reads as follows:

> *"The Consultant agrees to indemnify the Client from and against losses and damages to the extent they are found to be caused by an error, omission or negligent act of the Consultant under this Agreement."*

A useful clause recommended by Consulting Engineers Ontario[3] for clarifying the duty to defend, including interpretation of "hold harmless" is:

> *"Notwithstanding the duty to indemnify and hold/save harmless, the parties expressly agree that the Consultant has no duty to defend or fund or the defence of the Client/Indemnitees from and against any claims, causes of action, or proceedings of any kind. However, the Consultant expressly agrees, after adjudication by a court of competent jurisdiction, to reimburse the Client/Indemnitees pursuant to this provision for any costs and fees determined by court to have been reasonably, necessarily and actually incurred by the Client/Indemnitees in the defence of those claims specifically caused by the Consultant's negligence."*

This clause can be useful when a client is reluctant to remove a "defend" provision – they may be more comfortable doing so if clarifying language such as this is added to the agreement.

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[2] CCDC 31 – 2020 Service Contract Between Owner and Consultant. https://www.ccdc.org/document/ccdc31/
[3] Consulting Engineers Ontario. "Proceed Cautiously with Indemnity Agreements in Ontario-based Contracts" No. 20/003. March 13, 2020.

Other Considerations

There are other aspects consultants may need to consider in relation to indemnities, such as:

Limiting liability – if compelled to agree to a broad indemnity, focus on negotiating a reasonable limit of liability and suitable fees to account for the increased liability exposure. Indemnities and the limit of liability are key factors in assessing risks and making business decisions about whether to pursue an opportunity. Refer to the ACEC British Columbia Position Paper on Limitation of Liability for further details on this topic.

Assignment – proceed with caution if requested to indemnify a client's "assigns", i.e., a party or parties to whom the client may transfer their contractual rights. While details of assignment provisions are beyond the scope of this paper, each party should carefully consider assignment rights as part of contract negotiation.

Client indemnification of consultant – there are scenarios in which a consultant may wish to require indemnification from the client, e.g., when a consultant participates in a third-party review board, or during emergency situations such as flood relief or landslide response when insufficient data is available. Consultants may also require indemnification from a subconsultant as part of the flow-down of risk and liability.