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ATTORNEYS

THE LIABILITY OF DESIGN PROFESSIONALS

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I. BACKGROUND

The construction industry is undergoing a change in the landscape. While traditional methods of contracting still dominate, more and more projects are being completed and considered using alternative contracting structures such as "design-build" and "tri party agreements".

Even with traditional methods of contracting, emphasis is being placed on collaboration between the owner, the designer and the contractor. As a result, roles and responsibilities between the parties may be overlapping or blurred.

With this changing landscape, design professionals are also experiencing a legal shift in the interpretation and enforcement of certain legal doctrines and statutory immunities. The result has been an erosion of the protections historically afforded design professionals in the construction industry.

With this background, this paper evaluates the theories of liability for design professionals, the differences between contractor and design professional liability and closes with recommendations for minimizing claims.

II. LIABILITY IN CONTRACT

Design professional liability arises under contract when a contract is breached causing damages. Typically, this occurs when the scope of work may not be completed or when a particular clause in the contract is violated or ignored. On the other hand, when liability is based on tort, the claim alleges a breach of the professional standard of care.

a. Liability in Contract v. Liability in Tort

The distinction between a claim based on contract and a claim based on tort is significant when the statute of limitations is at issue. The statute of limitations for negligence actions is three years (RCW 4.16.080(2)) whereas the statute of limitations for breach of a written agreement is six years. RCW 4.16.040.

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Washington courts have indicated that a breach of the standard of care may also represent a breach of contract. *GW Construction Corp. v. Professional Services Industries, Inc.,* 70 Wn. App. 360 (1993) *review denied,* 123 Wn. 2d 1202 (1994) is instructive. In that case, the builder of a tilt up panel warehouse sued the engineer and characterized its claim as a breach of contract action to take advantage of the longer statute of limitations. The appellate court disagreed and stated that "[i]t does not necessarily follow that … each act required of a professional engineer utilizing reasonable engineering skill in the performance of a contract *ipso facto* constitutes a specific contractual undertaking." *GW Construction, 70 Wn. App.* at 364. In this particular case, the court reasoned that there was no written agreement that required the engineer to perform consistently with industry standards. *Id.*

Most design professional contracts include a clause that states the design professional will perform consistent with the standard of care of the profession and that no other warranties apply to this obligation. By specifying this standard in the contract, a breach of this standard not only triggers a negligence claim, but also a breach of contract claim.

b. Contract Formation

A significant exposure to design professionals can occur during the formation of the contract. It is not uncommon for owners to demand that the architect or engineer begin work without a signed contract. Sometimes, a contract may not be signed until close to the end of a project or it may not be signed at all. In both of those circumstances, the question becomes: What was the parties agreement? The general rule is that the courts will determine the "intent of the parties" subject to the parole evidence rule. *See Lynott v. National Union Fire Ins. Co.,* 123 Wash.2d 678, 871 P.2d 146 (1994)

This can often result in uncertainty and devastating results. In at least one unreported King County superior court case, a signed written contract between an engineer and an owner was held inapplicable because the contract was signed after the work was completed. The limitation of liability clause in the contract limited the engineer's liability to $5000. Since the written contract was held inapplicable, the engineer was exposed to over $750,000 in damages.

c. Other Common Issues Triggering Liability under Contract

Other areas that can create exposure to liability under contract relate to specific provisions that may be inserted in contracts such as (i) guarantees, (ii) warranties, and (iii) penalties for delays. Normally, these provisions are contained in agreements with contractors, and would not be applicable to the services of a design professional. However, if they do exist in executed

contracts, they will be applicable. This can arise most often in the alternative project delivery contracts discussed below.

d. Alternative Project Deliveries

While a significant majority of projects continue to be completed using traditional design-bid-build contracting mechanisms, over the past ten years, we have seen more and more projects being completed using a design-build mechanism, and more and more project participants are considering "integrated project delivery" ("IPD") and the use of tri-party contracting mechanisms. As the contract mechanisms change, so to do the potential contract liabilities.

i. Design-Build

Unlike traditional contracting mechanisms, in most design build contracts, the design professional is in a subcontract relationship with the contractor. These contracts generally take on two different forms. The first is when the owner has a design or at least the framework of a design that is part of the solicitation. In this instance, the design-build team is responsible for completing the design and constructing the project. The second is when the owner has no design, but has a "not to exceed" budget for the project. In this instance, the design build team must take on the entire responsibility for developing and completing the design and construction.

Under both scenarios, overlap occurs between the design and the construction, the contractor is intimately involved with the design, and no direct relationship exists between the design professional and the owner. As a result, while strong relationships between the members of the project team are critical to the success of design build projects, exposure under contractual liability theories potentially increases. This is because normal contractual protections are generally unavailable, no direct contractual relationship exists with the owner, and design and construction responsibilities can be blurred.

ii. IPD and Tri Party Agreements

In contrast to projects being completed under traditional contracting mechanisms, and design-build contracting mechanisms, very few projects have been completed using the multi-party agreements envisioned by the IPD process. In an IPD, the agreement usually includes three primary signatories: the owner, the contractor, and the design professional. The agreement creates interdisciplinary teams, tasked with high level management of the project as well as day-to-day management of the project. The agreement also creates a compensation structure that collectively rewards the parties for successfully achieving milestones on the project, and/or

completing the project under-budget and on-schedule. The signatories to a multiparty agreement are thus dependent on each other for profitability. Finally, many multiparty agreements require the parties to waive the ability to assert claims against each other as a means of limiting risk and litigiousness during the project.

With very little history on IPD projects, it remains to be seen whether the tri party agreements will reduce and minimize claims on construction projects. Contingency funds and insurance will become important parts of the contract. Not unlike design-build agreements, in tri party agreements the scopes and responsibilities between the parties can be blurred which can result in increased contractual liability exposure, notwithstanding the intent of the parties to collaborate on the project

III. LIABILITY IN TORT

Claims against design professionals in tort are normally based on negligence theories, although sometimes negligent misrepresentation claims are made. This section will focus only on the negligence theory.

a. Professional Negligence

The elements to prove professional negligence are:

i) Duty of Care (Professional Standard of Care)
ii) Breach of Duty
iii) Damages
iv) Proximately Caused by Breach

The professional standard of care is defined as the standard of care exercised by design professionals practicing in the same technical field for similar type projects in the same region and during the same time period.

A typical clause in a design professional contract relating to the standard of care is as follows:

> Design Professional agrees to provide Client, for its sole benefit and exclusive use, consulting services set forth in this Agreement. Design Professional's services shall be performed in accordance with the standard of care of its profession which means generally accepted professional practices, in the same or similar localities, related to the nature of the work accomplished, at the time the services are performed. Subject

to this standard of care, Design Professional makes no express or implied warranties regarding its services.

In determining what the standard of care is and whether it has been breached, the parties will rely on the expert testimony of similarly situated design professionals.

b. Economic Loss/Independent Duty

The Economic Loss, and now in Washington the Independent Duty, doctrine is a judicially-created mechanism for delineating tort claims from contract claims. Courts have historically considered the nature of claimed damages -- whether the damages are purely "economic" in nature or whether they involve injury to persons or other property -- in deciding the proper boundaries for tort and breach of contract claims. In Washington and most other jurisdictions recognizing the ELD, when the damages sought are essentially economic in nature (i.e., lost profits, cost overruns, project delays) and the parties have allocated the risk of economic loss in their contracts, the courts have held that only a breach of contract claim is permitted; as a consequence, only a party in contractual privity may recover from the party alleged to be at fault. On the other hand, when a claim involves an injury to a person or damage to other property, any injured party may assert a tort claim, such as professional negligence, against the responsible party, regardless of whether any contractual relationship exists between the two.

The leading case in Washington is *Berschauer/Phillips Constr. Co. v. Seattle School Dist. No. 1*, 124 Wn.2d 816, 881 P.2d 986 (1994). In *Berschauer,* the contractor incurred cost overruns on a construction project for renovation of a school and sued both the owner and the architect. The court articulated the primary issue as whether the economic loss rule prevented a general contractor from recovering purely economic damages in tort from an architect, an engineer and an inspector, none of whom were in privity of contract with the general contractor. In deciding in the affirmative, the court stated that its overriding concerns were protecting all of the parties' contractual expectancies and giving an incentive to negotiate risk. *In the context of complex multiparty transactions, at least, the preference for private ordering suggests that an engineer does not operate under extracontractual tort obligations*. *Id.*

In 2010, this "economic loss" doctrine was re-named the "independent duty" doctrine. The cases adopting this interpretation and limiting *Berschauer* were two cases consolidated before the Washington Supreme Court. *Eastwood v. Horse Harbor Foundation, Inc., et al.,* 170 Wn.2d 380, 241 P.3d 1256 (2010), and *Affiliated FM Insurance Co. v. LTK Consulting Services, Inc.,* 170 Wn.2d 442, 243 P.3d 521 (2010). The court, in these cases specifically preserved the holding in *Bershauer,* but appeared to revise the analysis to determine whether an "independent duty" exists as opposed to the previous analysis of determining whether purely economic damages exists.

The result of these cases is that the Economic Loss/Independent Duty doctrine has been significantly modified over the past several years. As articulated by the recent cases, if an independent duty exists, notwithstanding the existence of a contract, then a tort claim may

proceed regardless of whether the damages are economic or not, except that the ruling in *Berschauer* has been preserved. While construction defects represent "economic damages", that fact alone will not prevent the assertion of a tort claim for recovery of those damages against a design professional.

c. Limited Immunity for Construction Site Injuries

In Washington, and in most states, injured workers cannot sue their employers for workplace injuries. They can sue third parties if the third parties are at least partially at fault for the injuries. However, RCW 51.24.035 provides some immunity for claims against design professionals. Specifically, this statute provides:

> 1) Notwithstanding RCW 51.24.030(1), the injured worker or beneficiary may not seek damages against a design professional who is a third person and who has been retained to perform professional services on a construction project, or any employee of a design professional who is assisting or representing the design professional in the performance of professional services on the site of the construction project, unless responsibility for safety practices is specifically assumed by contract, the provisions of which were mutually negotiated, or the design professional actually exercised control over the portion of the premises where the worker was injured.
>
> (2) The immunity provided by this section does not apply to the negligent preparation of design plans and specifications.

In a 2011 case, *Larry Michaels, et. al. v. CH2M Hill,* 171 Wn.2d 587, 257 P.3d 532 (2011), the state supreme court interpreted this provision in the context of a fatal accident at a wastewater treatment plant. The court made several findings that could have profound effects on design professional liability. Specifically, the court concluded that making repairs or modifications on an existing facility does not constitute work at a construction site within the meaning of RCW 51.24.035. The court also concluded that "on-call" services and recommendations made at meetings can constitute the "preparation of design plans and specifications". Finally, the court concluded that, notwithstanding the lack of any control over the site or the safety of the owner's employees, the engineer still owed a duty of care that was breached and proximately caused the injuries.

While this case was grounded on very unique factual circumstances, it is uncertain as to whether this case will expand the traditional concepts of negligence as applied to design professionals.

IV. DESIGN PROFESSIONAL LIABILITY v. CONTRACTOR LIABILITY

Contractors and design professionals are normally subject to different liability theories based on their different roles in the construction process. Under traditional contracting scenarios, the

design professional is engaged first to prepare a schematic design followed by development of the actual design and then preparation of plans and specifications. Then, the contractor is engaged either through bidding on the construction documents, or negotiating a contract with the owner. The design professional remains involved during the bidding/negotiation phase, and then becomes active in construction administration by observing the activities of the contractor during construction.

The design professional generally enters into one contract for all of these phases (e.g., AIA B101-2007, Standard Form of Agreement between Owner and Architect). The design professional contract will typically disclaim warranties and clarify that the design professional will perform its work in accordance with the standard of care of its profession. The contract will also clarify that the design professional is only observing the activities of the contractor, and that it is not responsible for the means and methods of construction.

The contractor enters into a separate contract with the owner based on the contractor's cost for constructing the project in accordance with the plans and specifications. The contractor's contract contains warranties regarding the contractor's work and disclaims responsibility for design.

The result is that the liability of the contractor for design defects generally falls on the warranties and other promises in the contract. The design professional liability generally falls on whether the standard of care was breached and whether a duty was owed.

V. TIPS FOR MINIMIZING CLAIMS

a. Practice Tips

Design Professionals can adopt a number of practices that will protect against possible liability claims. These include:

i. Clear Scope of Work.

It is important to make sure the scope of work is clearly defined in the contract. In addition, the budget and cost needs to be adequate to cover the scope of work. When the scope is not well defined, or the budget is inadequate, a design professional may be subject to claims that certain tasks should have been completed without additional consideration. "Scope creep" can occur without adequate clarity in the contractual scope of work, which can lead to short cuts and exposure to professional liability claims.

ii. Relationships with Client and Project Team.

One of the most significant practices that will minimize claims is the establishment of good relationships with the client and the project team. With good relationships in place, participants are much more willing to work out problems rather than pointing fingers. The making of claims normally becomes a very last resort.

iii. Understanding On-site Responsibilities.

Claims sometimes arise because of the actions of on-site representatives. Normally, design professionals are not responsible for site safety or the actions of the contractor. However, this can certainly change if the actions of an on-site representative suggest otherwise.

iv. Other Practices.

Other practices that can reduce the number and significance of claims are (a) maintaining and implementing an effective quality assurance/quality control program, and (b) maintaining and implementing a good recordkeeping system that records important decisions and conversations.

b. Contract Provisions

Certain provisions can be negotiated and included in the contract. These include the following:

i. Limitation of Liability

Most design professional contracts contain some form of a limitation of liability clause. The purpose of this clause is to better allocate the risks and rewards of a project between the design professional and the design professional's client which normally is the project owner. A typical clause is as follows:

> Client expressly agrees that to the fullest extent permitted by law, Design Professional's maximum liability to Client for claims arising from Design Professional's professional acts, errors or omissions, shall be the amount of Design Professional's fee for professional services or _____, whichever is greater. In the event Client desires a higher limitation of liability, Design Professional may increase this limit for a higher fee commensurate with the increased risk to Design Professional, and this paragraph will be amended by separate written agreement. As used in this paragraph, the term "liability" means liability of any kind, whether in contract (including breach of warranty), in tort

(including negligence), in strict liability, or otherwise, for any and all injuries, claims, losses, expenses or damages whatsoever arising out of or in any way related to Design Professional's services or the services of Design Professional's subcontractors, consultants, agents, officers, directors and employees from any cause(s). Design Professional shall not be liable for any claims of loss of profits or any other indirect, incidental or consequential damages of any nature whatsoever.

The enforceability of these clauses depends on a variety of factors including whether the limitation is reasonable and whether the clause is clear and conspicuous. The courts generally interpret these clauses strictly and narrowly. These clauses represent negotiated terms and, therefore, only apply to the contracting parties and not to third parties.

ii. Indemnity

Indemnification clauses in design professional contracts are common. To align their insurance coverage with their potential liability, design professionals generally restrict their indemnification of the client to their negligence. In particularly risky projects, it is not uncommon for design professionals to seek the owner's indemnification for claims beyond the control of the design professional.
Last year, the state's anti-indemnification law was amended with the support of the design professional community. The revised law is as follows:

(1) A covenant, promise, agreement or understanding in, or in connection with or collateral to, a contract, or agreement relative to the construction, alteration, repair, addition to, subtraction from, improvement to, or maintenance of, any building, highway, road, railroad, excavation, or other structure, project, development, or improvement attached to real estate, including moving and demolition in connection therewith, **a contract or agreement for architectural, landscape architectural, engineering, or land surveying services**, or a motor carrier transportation contract, purporting to indemnify, **including the duty and cost to defend**, against liability for damages arising out of such services or out of bodily injury to persons or damage to property:

(a) Caused by or resulting from the sole negligence of the indemnitee, his or her agents or employees is against public policy and is void and unenforceable;

(b) Caused by or resulting from the concurrent negligence of (i) the indemnitee or the indemnitee's agents or employees, and (ii) the indemnitor or the indemnitor's agents or employees, is valid and enforceable only to the extent of the indemnitor's negligence and only if the agreement specifically and expressly provides therefor, and may waive the indemnitor's immunity under industrial insurance, Title 51 RCW, only if the agreement specifically and expressly

> provides therefor and the waiver was mutually negotiated by the parties. RCW 4.24.115 (emphasis added).

The specific amendments are bolded above. Specifically, the statute was amended to clarify that it also applies to contracts with design professionals, and that the statute not only prohibits indemnification, but also a duty to defend or payment of defense costs in the cases identified in (1)(a) and (b) of the statute.

iii. Other Contractual Protections.

Other important contractual provisions and protections include creating a contractual time bar for legal actions that is more restrictive than statutory limitation periods and specifying in the contract those items or work scopes that will not be performed. Both of these provisions can provide very significant opportunities for reducing and eliminating claims.

IV. CONCLUSION

The landscape of construction projects is undergoing significant change with more and more efforts being made to enhance collaboration between all of the project participants. With this changing landscape comes a potential overlap and blurring of the roles and responsibilities of the ownership team, the construction team and the design team. This creates the potential for exposure to liabilities not normally assumed by design professionals.

At the same time, the legal landscape in Washington is changing with the erosion of protections normally relied upon by design professionals. The result may be that now, more than ever, design professionals must understand their potential exposure and establish risk management programs accordingly. In addition, design professionals may be more inclined to prepare more conservative designs and practice "defensive" engineering. With the inception of more alternative project delivery contracting mechanisms, it remains to be seen as to whether these contracting and delivery methods will actually reduce the number and severity of claims.