

Department of Legislative Services
Maryland General Assembly
2022 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 79
Judiciary

(Delegates Cardin and Atterbeary)

Courts - Prohibited Indemnity and Defense Liability Agreements

This bill expands the prohibitions in § 5-401 of the Courts and Judicial Proceedings Article against certain agreement clauses in construction or construction-related contracts by prohibiting the inclusion of (1) specified indemnification or hold harmless clauses and (2) specified provisions requiring a “design professional” to defend parties against liability or certain claims. The prohibitions in § 5-401, as amended by the bill, may not be interpreted to prohibit an otherwise enforceable indemnity or hold harmless provision from including recovery of reasonable attorney’s fees and defense costs under specified circumstances. The bill also incorporates contracts or agreements relating to highways and roads into existing statutory prohibitions.

Fiscal Summary

State Effect: The bill may have an operational effect on State agencies and increase State expenditures, as discussed below.

Local Effect: The bill may have an operational effect on local governments and increase local expenditures, as discussed below.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The bill prohibits the inclusion of indemnification or hold harmless provisions in, or in connection with, contracts or agreements with a design professional for “professional services.” The prohibition exists unless the fault (as that term is defined in

the bill) of the design professional or its “derivative parties” is the “proximate cause” of the loss, damage, or expense indemnified.

The bill also prohibits any clause requiring the design professional to defend a promisee or any other person against liability or claims for damages or expenses, including attorney’s fees, alleged to be caused by the professional negligence of the design professional or its derivative parties. This type of clause is void and unenforceable and against public policy.

Section 5-401, as amended by the bill, may not be interpreted to prohibit an otherwise enforceable indemnity or hold harmless provision in any contract or agreement from including recovery of reasonable attorney’s fees and defense costs (as that term is defined in the bill) actually incurred by the promisee to defend against third-party claims for damages, losses, or expenses in cases where the fault of the promisor or its derivative parties is determined to be the proximate cause of the defense costs to be indemnified.

A “design professional” is a licensed architect, certified interior designer, licensed landscape architect, professional engineer, or professional land surveyor.

“Derivative parties” means a party’s subcontractors, agents, employees, or other persons for which the party may be liable or responsible as a result of any statutory, tort, or contractual duty.

Current Law: At common law, a contract can be unenforceable if it has an illegal purpose, is contrary to public policy, or is unconscionable, among other reasons. In general, under § 5-401 of the Courts Article, construction or property maintenance contracts or agreements indemnifying the promisee against liability for damages resulting from the sole negligence of the promisee or indemnitee, or their agents or employees, are against public policy and are void and unenforceable. This prohibition also applies to architectural, engineering, inspecting, and surveying services.

Also, with respect to these same types of contracts or agreements, an agreement to defend or pay the costs of defending promisees or indemnitees against liability for damages arising out of bodily injury to any person or damage to property caused by or resulting from the sole negligence of the promisee or the indemnitee, or their agents or employees, is void and unenforceable as a matter of public policy under State law.

However, these prohibitions do not apply to an insurance contract, a general indemnity agreement required for a surety bond, worker’s compensation, or any other agreement issued by an insurer.

State Fiscal Effect: The bill has an operational effect and *may* result in increased litigation expenditures for affected State agencies. Due to the irregular occurrence of these claims

and the broad range and complexity of potential claims, potential expenditures under the bill cannot be reliably determined at this time.

According to the Maryland Transportation Authority (MDTA), the indemnification and duty to defend provisions under § 5-401(a)(4) and (a)(5) of the bill are standard provisions contained in its design professional and construction contracts. MDTA advises that the proposed legislation may have an impact on MDTA, but the amount is not determinable. While claims involving construction contracts do occur periodically, MDTA cannot recall a claim involving a design professional in at least 11 years.

According to MDTA, the bill (1) requires MDTA to change its existing contract language; (2) imposes a higher standard (proximate cause) before seeking indemnity from specified types of vendors/contractors; and (3) requires MDTA to defend claims initially and then seek reimbursement for costs of defense if the contractor is determined to be the proximate cause. Current MDTA contractual language requires a contractor to indemnify MDTA/State for actions “arising out of or resulting from [their] errors, omissions, negligent acts...” Also, under the current “duty to defend,” the Office of the Attorney General counsel within MDTA acts in a consulting capacity; the bill requires MDTA to take a more active role in its legal defense, as discussed above.

The State Highway Administration (SHA) does not anticipate a fiscal impact from the bill. However, provisions in SHA’s requests for proposals appear to contain indemnification language that is similar to MDTA’s contractual language.

According to the Department of General Services (DGS), which is the control agency for architectural and engineering procurements, indemnity is a legal and equitable remedy that, when negotiated, will alleviate the State from having to pay out claims and damages that were not the State’s fault but the fault of the consultant, contractor, or other party. However, DGS also acknowledges that with the exception of instances involving patents, copyrights, and records, its architectural and engineering contracts do *not* contain the clauses rendered void and enforceable under the bill.

The Treasurer’s Office (STO) advises that the bill does not have a fiscal impact on claims paid out of the State Insurance Trust Fund. According to STO, economic damages would be generally included as part of any bodily injury or property damage claim and paid if the State were negligent. STO is unaware of any claims whereby the State was negligent but was able to pass the economic losses off to a State contractor.

Local Fiscal Effect: To the extent that local government contracts contain provisions affected by the bill, the bill may have an operational effect on local governments and may increase local expenditures.

Small Business Effect: The bill has a meaningful impact on small businesses that have entered into these types of agreements and that, as a result of the bill, (1) no longer have to indemnify, legally defend, or pay losses, damages, or expenses for a promisee/indemnitee or (2) are no longer indemnified or no longer have their losses, damages, or expenses provided/funded by a promisor/indemnitor.

Additional Information

Prior Introductions: HB 213 of 2021 received a hearing in the House Judiciary Committee, but no further action was taken. SB 189, its cross file, received a hearing in the Senate Judicial Proceedings Committee, but no further action was taken. HB 681 of 2020 received a hearing in the House Judiciary Committee, but no further action was taken. SB 368, its cross file, received a hearing in the Senate Judicial Proceedings Committee, but no further action was taken.

Designated Cross File: SB 161 (Senator West) - Judicial Proceedings.

Information Source(s): Maryland State Treasurer's Office; Judiciary (Administrative Office of the Courts); Department of General Services; Maryland Department of Transportation; Department of Legislative Services

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