ACEC-MD_FAV_SB368
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Position: FAV

ACEC

American Council of Engineering Companies
Maryland

SB 368 Courts – Prohibited Indemnity and Defense Liability Agreements

SUPPORT

ACEC/MD is a nonprofit association headquartered in Baltimore with over 90 multi-sized consulting engineering firms located throughout the state serving the public as well as private sectors. Forty five percent of ACEC/MD's members are certified minority or women-owned firms or small businesses. Member firms employ approximately 7000 employees and are responsible for the design of most of the area's infrastructure, environmental and building construction.

ABOUT THE BILL: After a claim is adjudicated, the insurance policy of the responsible party is normally expected to pay for the indemnity and defense costs. If there are multiple responsible parties, the insurers representing each party will normally negotiate an equitable distribution of the claim costs.

The members of ACEC/MD do not believe that expecting an a design professional (engineering firm) to pay the indemnity and the defense costs on claims, where they bear no responsibility for the proximate cause of the injury or loss, is a normal insurance practice.

Contracts for design professionals often include provisions that require the design professionals to assume the liability for the indemnity and the defense costs that would normally be attributed to the promisee (owner). The design professionals who refuse to accept these provisions are excluded from bidding on these contracts.

Attached is an exhibit that explains why insurance underwriters are unwilling to pay for claims and legal expenses that are not attributed to some fault on the part of policy holder. If an design professional agrees to a contract with the provision in question they are exposed to significant uninsured liability. Such payments can adversely affect the ability of the design professional profitability and eventual solvency.

You may ask why do design professionals and many others sign such contracts? In most instances, they have no alternative *(an unfortunate reality that exists where large entities contract with powerless providers).* Should the state allow the of use of inequitable contracting practices to coerce private business into accepting unknown, possibly incapacitating risk so the state can lower its insurance premiums?

The members of ACEC/MD believe the amendments in SB 368 are not unreasonable changes in public policy for Maryland.

These changes are limited to determining which insurance carrier(s) should be responsible to pay the indemnity and defense costs. As written the amendments do not inhibit the filing of claims, or limit the reasonable liability of those responsible, nor reduce the awards payable to any claimant.

Design professionals are willing to assume any liability that can be attributed to their performance and that of their derivative parties, which is the proximate cause of the loss, damage or expense indemnified.

Likewise, once fault is attributed, the design professional will assume the responsibility to reimburse the owner for legal fees and defense costs.

A favorable vote on SB 368 would be most appreciated

312 N. Charles St. (Ste. 200) ❑ Baltimore, MD 21201 ❑ (410) 539-1592 ❑ acecmd@acecmd.org

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Uploaded by: Otradovec, James
Position: FAV

7. Indemnity

An indemnity is a common contractual risk-shifting mechanism. To indemnify means to assume a specific liability in the event of a loss. As a basic principle of negligence law, the design professional is legally liable for damages caused as a direct consequence of its negligent acts or omissions, which is exactly what is covered by a design professional's professional liability insurance policy. Accordingly, it is very important that the design professional agrees to indemnifications that are limited to only to those damages that are directly and proportionally attributable to the negligent performance of professional services. Indemnity clauses should have the following characteristics:

- Be fair and insurable, for the benefit of the owner and its defined representatives only, not "agents" or any other parties
- Be negligence-based and to the proportionate extent caused by negligent performance of services
- Not include or delete the word "defend". However, in California and potentially other states, not including or deleting the word "defend" is not enough. In California and potentially other states, the contract must specifically express that there is no duty to defend, and the wording must meet the governing state's legal standards and requirements in order for it to be upheld. The duty to defend another is not generally insurable under a design professional's liability insurance policy. It is considered a contractually assumed liability, which is typically excluded from PL insurance coverage.
- Be properly drafted in accordance with the state laws applicable to the project. Enforceability of indemnity provisions vary by state and wording that is acceptable and enforceable in one state may violate anti-indemnity statutes in another state.
- Provide for indemnification of reasonable attorneys' fees and expenses but only if recoverable by law in the applicable jurisdiction. Specifically exclude defense obligations prior to and in the absence of a finding of fault. If the attorneys' fees and costs would be awarded to the Client only because of the contract, and not because of governing law, it is considered a contractually assumed liability that is not insurable under a design professional's liability insurance policy.

Example language: *The Consultant shall indemnify and hold the Client and the Client's officers and employees harmless, but not defend, from and against damages, losses and judgments arising from claims by third parties, including reasonable attorneys' fees and expenses recoverable under applicable law, but only to the extent they are caused by the negligent acts or omissions of the Consultant, its employees and its consultants in the performance of professional services under this Agreement. The Consultant has no obligation to pay for any of the indemnitees' defense related cost prior to a final determination of liability or to pay any amount that exceeds the Consultant's finally determined percentage of liability based upon the comparative fault of the Consultant, its employees and its consultants.*

WEST_FAV_SB368
Uploaded by: West, Chris
Position: FAV

CHRIS WEST
Legislative District 42
Baltimore County

Judicial Proceedings Committee

Vice Chair, Baltimore County
Senate Delegation

THE SENATE OF MARYLAND
ANNAPOLIS, MARYLAND 21401

Annapolis Office
James Senate Office Building
11 Bladen Street, Room 303
Annapolis, Maryland 21401
410-841-3648 · 301-858-3648
800-492-7122 *Ext.* 3648
Chris.West@senate.state.md.us

District Office
1134 York Road, Suite 200
Lutherville -Timonium, MD 21093
410-823-7087

February 12, 2020

Senate Judicial Proceedings Committee
The Honorable William C. Smith, Jr.
2 East Miller Senate Building
Annapolis, Maryland 21401-1991

RE: SB 368 – Courts – Prohibited Indemnity and Defense Liability Agreements

Dear Chairman Smith and Members of the Committee:

I am pleased to introduce Senate Bill 368.

In connection with a construction project, there are generally numerous contracting parties. There is the owner, the contractor, the architect, the engineer, subcontractors and other professionals. When an accident occurs resulting in significant losses, the responsible party and/or its insurance carrier is normally expected to pay for the damages. Where there are multiple defendants, there may be multiple insurers. In this situation the insurers will usually negotiate an equitable allocation of the losses.

But there are situations in which the owner of the project or the prime contractor is so dominant that it can force the architect and the engineer associated with the project to execute contracts containing an onerous provision requiring the design professional firm to indemnify the owner or the prime contractor, as the case may be, for all of the damages and expenses associated with the loss, irrespective of the fact that the design professional firm was not the proximate cause of the loss. Of course, the design professional firm has its own insurance, but the insurance companies issuing insurance to design professionals customarily refuse to reimburse them for any indemnification payments to the owner in such situations because the losses were not proximately caused by the design professionals. So the design professionals in these situations end up shouldering the burden of paying all of the losses resulting from an accident, including all of the attorney's fees associated with the trial of the case, even though the design professional were not the proximate cause of the loss.

Fortunately, contracts containing such clauses are not customary. But some Maryland State procurement contracts and some other construction contracts used by very large construction companies contain such indemnification provisions. These are virtually contracts of adhesion because the design professional firm knows that if it wants the work, it will have to sign an unfair contract.

Now let me discuss Senate Bill 368. Maryland law currently provides that a provision in an architectural or engineering contract purporting to indemnify the other party to the contract for damages arising due to the ***"sole negligence"*** of the other party is against public policy and is void and unenforceable. Maryland law also currently provides that a provision in an architectural or engineering contract purporting to require the design professional firm to pay for the costs of defending the other party to the contract against liability for damages resulting from the ***"sole negligence"*** of the other party is against public policy and is void and unenforceable.

Senate Bill 368 just adds language to the existing statute stating that a provision in an architectural or engineering contract requiring the design professional to indemnify the other party to the contract against loss is void and unenforceable unless the fault of the design professional is ***the proximate cause*** of the loss. In other words, under the new language added by Senate Bill 368, the design professional can only be required to indemnify the other party to a contract if the fault of the design professional is ***the proximate cause*** of the loss but not if the design professional was not the proximate cause of the loss.

Finally, Senate Bill 368 adds two additional provisions dealing with the obligation of the design professional firm to pay the attorney's fees and other defense costs of the other party to the contract attributable to an allegation of liability. They provide that the design professional will not have to pay for such costs until such time as a determination is made that the fault of the design professional is ***the proximate cause*** of the defense costs. At that point, the design professional will have to indemnity the other party to the contract for all reasonable attorney's fees and other defense costs.

I urge a favorable report on Senate Bill 368.

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Uploaded by: KEMERER, HANNIBAL
Position: UNF

BRIAN E. FROSH
Attorney General

ELIZABETH F. HARRIS
Chief Deputy Attorney General

CAROLYN QUATTROCKI
Deputy Attorney General

STATE OF MARYLAND
OFFICE OF THE ATTORNEY GENERAL

FACSIMILE NO.
410-576-7036

WRITER'S DIRECT DIAL NO.
410-576-6584

February 12, 2020

TO: The Honorable William C. Smith, Jr.
Chair, Judicial Proceedings Committee

FROM: The Office of the Attorney General

RE: SB 368 – Courts – Prohibited Indemnity and Defense Liability Agreements
(OPPOSE)

The Office of the Attorney General urges this Committee to issue an unfavorable report on SB 368. If enacted, this legislation would eliminate all but two causes of action, negligent performance or breach of contract, that Maryland might seek to bring against architects, certified interior designers, landscape architects, professional engineers, or professional land surveyors with whom it contracts. The bill would make indemnity clauses in government contracts that bind government contractors "against public policy and . . . void and unenforceable." See Section 5-401(a)(5).

In two cases handled by the Office's Contract Litigation Unit several years ago, the State was fully indemnified by the project architect for the architect's errors and omissions insurer for damages resulting from errors in building design and, in the one case, ambiguous drawings. In one of those matters, the architect failed to prepare design drawings that complied with the applicable code requirements for the building's seismic loading. The building's contractor submitted claims totaling nearly $1.7 million for delay and direct costs as a result of those errors and ambiguities, and the architect paid $350,000 directly to the contractor to resolve the matter. In the other, the project architect's structural engineer discovered, after contact award to the building contractor, that certain structural changes should have been made during the final check of the contract's structural drawings before bid but were overlooked and not incorporated into the final contract drawings issued for bid. In that case, the project architect and structural engineer paid $163,000 directly to the contractor in order to resolve the matter. Liability in these matters would be less clear and more susceptible to challenge if SB 368 were to become law.

Proponents of SB 368 suggest that various Maryland Departments require procurement contracts to include clauses binding architects and engineers, among others, to indemnify the State for misconduct, negligence, or breaches that neither the architects nor engineers committed. In their view, the legislation is intended to ensure that public procurement contracts do not alter or elevate the legal liability of architects and engineers with respect to their performance of professional services for public clients. However, Maryland's requests for proposals (RFPs)—regardless of Department—are not contracts of adhesion. No business entity is forced to bid on Maryland RFPs, nor, upon bidding, are they forced to enter into contracts. Providing professional services to the State can prove lucrative. Knowing this, Maryland is best served by insisting upon contracts that best protect its interests. Legislating to eliminate potential causes of action against architects and engineers, among others, is not in Maryland's best interest. Therefore, for all of the foregoing reasons, the Office of Attorney General urges an unfavorable report on SB 368.

cc: Members of the Judicial Proceedings Committee

DGS_INFO_SB368
Uploaded by: Swygert, Michael
Position: INFO

Larry Hogan
Governor

Boyd K. Rutherford
Lt. Governor

Ellington E. Churchill, Jr.
Secretary

MARYLAND DEPARTMENT OF GENERAL SERVICES
OFFICE OF THE SECRETARY

BILL: **Senate Bill 368**
Courts – Prohibited Indemnity and Defense Agreements

COMMITTEE: Senate Judicial Procedures

DATE: February 12, 2020

POSITION: Letter of Information

Upon review of Senate Bill 368 – Courts – Prohibited Indemnity and Defense Agreements, the Department of General Services (DGS) provides these comments for your consideration.

Senate Bill 368 holds that a provision within an architectural or engineering services (A/E) contract or agreement protecting the State against loss, damages or expenses is void and unenforceable unless the design professional is the proximate cause of the loss, damage or expense. Further, Senate Bill 368 holds that a provision within a contract or agreement protecting the State against damages or expenses due to an A/E's negligence is against public policy and is void and unenforceable.

Senate Bill 368 shifts the risk within an A/E contract to the State from the hired design team. Senate Bill 368 limits the State's ability to be indemnified in only certain instances. Indemnification is already required in purchase orders over $25,000.

It is important to note that indemnity is a negotiated provision that is available to the State, it is a legal and equitable remedy, and when negotiated it will alleviate the State from having to pay out claims or damages that were not the State's fault but the fault of a consultant, contractor or other party. In addition, DGS' current A/E contracts do not have an indemnification clause, except for instances involving patents, copyright, and records. Consequently, DGS did not have an indemnification clause in its prior A/E contracts and there have not been any issues with the A/E's nor with the A/E's securing insurance or bonding.

For additional information, contact Ellen Robertson at 410-260-2908.

301 West Preston Street
Baltimore, Maryland 21201-2305
(410) 767-4960
FAX (410) 333-5480

Toll Free 1-800-449-4347
e-mail: Ellington.Churchill@maryland.gov
TTY users 1-800-735-2258