# International Municipal Lawyers Association
## 75th Annual Conference

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## OWNER'S FIELD GUIDE TO RISK TRANSFER PROVISIONS IN MODERN DAY DESIGN AND CONSTRUCTION CONTRACTS

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**Presented at the 2010 Fall Meeting**

**IMLA Puttin' the Law Back in JambLAWya:**
**Still HOT after 75 Years!**

**October 10-13, 2010**
**Hilton New Orleans Riverside Hotel, New Orleans, Louisiana**

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## INTRODUCTION

Don't give up on this paper just yet. We know the subject is a tad dry, but give us an opportunity to convince you otherwise.

The anatomy of any modern design and construction agreements , at their essence, can be divided into four (4) primary parts:

(1) Provisions dealing with cost;

(2) Provisions dealings with time;

(3) Provisions defining the scope or deliverable; and

(4) Provisions dealing with risk or risk transfer.

This paper deals with the fourth category of provisions, and from a construction lawyer's perspective, these provisions are frequently the most critical components of the agreement. They are the provisions that spell the difference in a project if things do not go as expected, which is the precise time that your mayor, city manger or other management type, will be looking to you for answers --- and good answers at that. Rather than give you a boring, staid academic paper, we have tried to take things in a different direction and give you a practical "field guide" to risk shifting provisions that you encounter day to day in your projects. What we have done is profile six (6) risk transfer provisions in this way:

First: We introduce the subject (like Indemnity or Builder's Risk) and describe what the topic means in plain English. Second: We describe a case where an Owner came close or experienced a very harsh result after failing to carefully negotiate a key risk provision. Third: We give you a takeaway and advice that dovetails with our PowerPoint presentation.

Before we dive in, a final point: Form construction agreements published by professional societies like the American Institute of Architects ("AIA") or Engineer Joint Contract Documents Committee ("EJCDC") dominate the public sector. There are good reasons for that (cost and chiefly speed), of course. The problem with the form agreements from the owner's perspective, however, is that they "bear the bias" of their publishers and tend to favor the designer's and builder's interests. Of course, modification of the AIA or EJCDC forms is common and logistically easy to accomplish. Owners who fail to seize the opportunity to modify these custom agreements leave their wallets on the table. Your designer's comments about the agreements being "standard" and never altered are simply false. Let your designers give you engineering and architectural advice – get your legal counsel elsewhere.

## I. INDEMNITY PROVISIONS

### *A. What is Indemnity? It's kind of like insurance – but not.*

An indemnity provision is a clause in a contract that requires one contracting party to pay the legal liabilities of the other party under certain circumstances. Construction contracts often require the general contractor to indemnify the owner with respect to the owner's liability to members of the public who are injured or whose property is damaged during the course of the contractor's work. The purpose of an indemnity provision in a construction contract is to contractually allocate the risk of third-party liability claims between project participants.

You may wonder what the difference is between an indemnity provision in a construction contact and an insurance policy. While insurance is a *form* of indemnity, an indemnification provision in a construction contract does not create an insurer/insured relationship between the parties. Importantly, indemnity provisions and insurance contracts are not interpreted in the same manner under the law. Because indemnity provisions are typically disfavored under the

law (much more than insurance policies), you as an Owner should take special care in drafting the indemnity provision in your agreements with your general contractors so as to protect yourself from "falls" like the one taken by the owner in the case discussed below.

***B. A Cautionary Tale of Taking the Fall, Literally and Figuratively.***

In *Gomez v. Sharon Baptist Board of Directors*[1], a construction worker filed a lawsuit against a property owner after the worker fell from a scaffold on the owner's property and injured himself. The scaffold wheels had not been locked and the worker had not been provided with safety equipment. The worker claimed violations of labor laws against the owner, and the owner was held liable as a function of the applicable labor laws. (Of course, as a practical matter, the owner was not the one who unlocked the scaffold wheels, or the one who instructed the worker to climb up on the scaffolding with unlocked wheels, or the one who instructed the worker to climb up on the scaffolding with unlocked wheels with no safety equipment – you get the picture.)

The owner filed a claim against the worker's employer, a general contractor, seeking indemnification pursuant to their written agreement. The owner and the general contractor had contractually agreed that the general contractor was obligated to indemnify the owner for losses to the extent that they were caused in whole or in part by the general contractor's negligent acts or omissions – which is pretty standard form language for indemnity provisions in owner-contractor agreements.

On summary judgment, the trial court ruled against the owner on its indemnification claim, finding that the owner's liability to the worker under the labor laws (as well as its only basis for indemnification) had absolutely nothing to do with the general contractor's negligence. Rather, the owner's liability to the work was simply assigned to the owner by virtue of the

[1] 55 A.D.3d 446 (N.Y. App. Div. 2008).

function of the applicable labor laws. As a result, the construction worker was not the only party who took a fall. Stuck with the form language in its written agreement with the general contractor, the owner took a figurative fall of its own, and the general contractor at this stage in the litigation escaped scot-free.

### *C. Takeaway: Indemnity Provisions*

Well written indemnity requirements in owner-contractor agreements should provide maximum protection to the owner without being onerous to the general contractor. No doubt, this is not an easy task. Savvy owners must balance risk allocation with budget constraints, knowing that contractors will increase their normal charges to reflect increased risks if the owner's indemnity requirements are unreasonable. Balance is critical.

Do not let yourself be blindsided by liability like the owner in the *Gomez* case, who likely unknowingly and passively signed a form agreement with a watery indemnification clause. Negotiate for the coverage necessary for your comfort and for your project at the start of the relationship with the general contractor, when your bargaining power is perhaps the strongest it will be during the relationship.

## II. WAIVERS OF SUBROGATION

### *A. What is a Waiver of Subrogation Anyway (aside from a Seemingly Boring Topic)?*

A waiver of subrogation is another type of risk-shifting provision in a contract, dealing with an insurer's right to seek recourse after having made a payment to an insured following a loss. It allows parties to waive their rights to claim damages against one another up to the amount of insurance coverage available for their losses. Parties use them to substitute the certainty of an insurance recovery for the uncertainty of litigation or arbitration. In the property insurance context, owners subrogate their claims to insurance companies and, in some instances,

the insurance company will assign its subrogation rights back to the owner.[2] Insurance companies generally dislike subrogation waivers and may prohibit owners from waiving their rights to recovery against those causing a loss.

If you are looking for official confirmation that the subject of subrogation waivers is one that is superficially boring, we hear you. One California court has described the examination of issues related to subrogation waivers as follows:

> The fact remains that the issues are far from enthralling; they demand an almost microscopic examination of dry, lengthy contract documents. As we embark on the resolution of these issues, then, we think it only fair to suggest that the reader might want to be sitting in a comfortable chair, with a cup of strong coffee nearby.[3]

Nevertheless, when an Owner prepares and signs a contract containing a subrogation waiver, knowledge about subrogation waivers is just as critical as the subject is dry, as illustrated by the cautionary tale below.

### *B. A Cautionary Tale: How Something As Mundane As a Subrogation Waiver Caused an Owner Seven Years of Unwelcome "Excitement" and Expense.*

The facts of a case that reached the Colorado Supreme Court provide a cautionary tale for Owners with regard to subrogation waivers. In *Copper Mountain, Inc. v. Industrial Systems, Inc.*[4], a ski resort owner hired a general contractor to renovate and expand the ski lodge. The general contractor subcontracted with a welder to build the steel framework for the addition. The owner and the general contractor entered into a standard AIA owner-contractor agreement to govern the construction.

Putting aside the tedious definitions and conditions in the AIA contract for purposes of this discussion, suffice it to say that in this case, the owner of the ski lodge agreed to waive its

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[2] *Copper Mountain, Inc. v. Industrial Systems, Inc.*, 208 P.3d 692, 693 n.2 (Colo. 2009).
[3] *American Guarantee & Liability Insurance Company v. ADP Marshall, Inc.*, 2007 WL 4239987, *1 (Cal. Ct. App. December 4, 2007).
[4] 208 P.3d 692 (Colo. 2009)

subrogation rights. More specifically, the owner waived its rights against the general contractor to recover damages caused by fire to the extent the property was covered by property insurance.

As luck would have it (or not), a fire broke out at the lodge while the subcontractor was performing its welding work. The fire caused significant damage to the ski lodge and its contents. Adding insult to injury, at least some of fire damage to the lodge was to areas that were *not* part of the project, which in this case meant that the owner had to go to court to find out whether its waiver of subrogation rights applied to these areas that were not part of the renovation and expansion project. In other words, the owner had to spend a substantial amount of money to have a court decide whether the owner had a right to pursue damages against the general contractor and subcontractor for the fire damage at the lodge.

In an attempt to recover damages from the fire, the owner filed a lawsuit against both the general contractor and the subcontractor. Unfortunately for the owner, the trial court ruled against it, holding that the owner's waiver of subrogation barred the owner's claims against the general contractor and the subcontractor for the fire-related damages. The owner appealed the trial court's ruling and again, it did not get the answer it wanted from the appellate court, which upheld the trial court's decision. Appealing again, this time to the Colorado Supreme Court, the owner finally got some relief: The Colorado Supreme Court reversed the trial court and appellate court's rulings, instead finding that the owner's waiver did *not* extend to property not considered the work of the project.[5]

Although this case ended favorably for the owner, it is not difficult to imagine that the owner was probably not terribly excited about the expense of obtaining the result. Certainly the owner spent a small fortune pursuing the general and sub- contractors. Perhaps worse is the fact that more than *seven years* of time passed after the fire before the owner, at long last, had in hand

[5] *Id.* at 700.

the final ruling from the Colorado Supreme Court. Thankfully this final ruling was in the owner's favor, but the owner spent the majority of those seven-plus years fighting off *un*favorable rulings handed down by the trial court and the appellate court. Ouch.

### *C. Takeaways: Subrogation Waivers*

The moral of this story is that when an owner is contracting for work on existing structures and agrees to a subrogation waiver, the owner should emphasize that the waiver extends only to the project's work. The owner should be very careful to include the appropriate language to protect itself against damages caused during project work to other parts of the building that are not part of the project, as defined in the construction agreement.

If you as the Owner of a project are not particularly well-versed in the ins-and-outs of subrogation waivers, you are best served to find someone with working knowledge of subrogation waiver provisions to provide you an edge to protect yourself and your project from an awful lot of trouble, on both the time and money fronts. These details should be hashed out on the front end of a project. Do not put yourself in a position to where you are at risk of spending over seven years fighting about what the provision covers.

## III. WAIVERS OF CONSEQUENTIAL DAMAGES

### *A. What's the Harm?*

Construction damages are commonly divided into two general categories: direct damages and consequential damages. Direct damages are those that have a direct causal connection to the breach. For instance, when a contractor defectively constructs a property, the direct damage is either the cost of repairing the property or the diminution in value of the property. Consequential damages go beyond merely rectifying the defective construction and are awarded to compensate the non-breaching party for all the foreseeable damages stemming from the breach.

A contractor's breach may force the owner to delay opening the facility, reduce revenue, decrease profits, hurt the owner's reputation, and force the owner to encounter significant management and oversight costs stemming from the defective performance. As a result, owners often feel that direct damages inadequately compensate them for their losses.

The 2007 AIA A201 General Conditions of the Contract for Construction waives claims for consequential damages. Included in the AIA's waiver of consequential damages include damages "for rental expenses, for losses of use, income, profit, financing, business and reputation, and for loss of management or employee productivity or of the services of such persons."[6]

When the owner accepts this waiver, the owner handcuffs his ability to adequately protect his interests. While the philanthropist in each of us may argue that profits, income, expenses, and similar pecuniary remuneration remains irrelevant, the balance sheet unfortunately remains detached from such noble undertakings. Thus, if the owner's balance sheet is of any consideration, the prudent owner will NOT waive consequential damages.

### *B. A Cautionary Tale*

One case illustrating the follies associated with a waiver of consequential damages is *Cryogenic Equipment, Inc. v. Southern Nitrogen, Inc*.[7] In *Cryogenic*, the owner wanted to build the standard run-of-the-mill nitrogen-liquification plant. The parties, understanding the complexities of nitrogen-liquification plants, inserted a mutual waiver of consequential damages similar to the one provided by the AIA form documents.

The contractor, unfortunately, defectively constructed the plant causing numerous delays and reducing the owner's ability to engage in nitrogen liquification. The owner estimated that the

[6] AIA Doc. A201.
[7] 490 F.2d 696 (8th Cir. 1974).

contractor cost the owner approximately $700,000 in lost profits, delay damages, and other consequential damages.

The owner sued the contractor for the damages and the court denied all consequential damages. The court held that the owner was limited in recovery to the costs of repairing the defective facility, but refused to award any damages related to delay, lost profits, or other consequential damages due to the mutual waiver. Thus, as a result of the contractor's breach, the owner was essentially forced to bear the costs of the contractor's defects.

### *C. Takeaway: Don't Waive Consequential Damages (Unless Recourse Against Your Contractor is Not Something You Care About)*

Mutually waiving consequential damages is typically not in the owner's best interest. The owner has much greater potential for loss than the contractor. Additionally, the owner's exposure is typically much greater than the contractor's. Accordingly, mutual waivers of liability are in the contractor's best interest.

By waiving consequential damages, the owner bears the risk of lost profits, lost revenue, lost income, and lost business reputation when it is far less able to control those risks than the Contractor. Accordingly, in order to adequately protect the owner's interest, the owner should not waive consequential damages. Tell your Contractor you simply want the ability to pursue the damages allowed by the law of your state – nothing more and nothing less.[8]

[8] The mutual waiver of consequential damages which has been added to both the owner-contractor contract and the owner-architect agreement by the 1997 revision of the AIA form set, and retained in the 2007 set, may be a problem for a public entity such as a local government. Generally, absent charter language to the contrary, some state public entities (such as Tennessee) cannot waive any legal rights they might have. Therefore, a public entity may not be legally empowered to waive consequential damages.

## IV. BUILDERS' RISK PROVISION

### *A. Why Do We Need Builders' Risk Insurance?*

Most construction contracts require that the owner insure the property while it is under construction. Builders' Risk policies provide this coverage. These policies provide first party, no-fault, insurance against the risk of loss to construction projects.

Risk allocation is particularly important for construction projects due to the inherent riskiness of the projects. As compared to completed structures, projects under construction are far more susceptible to loss or damage stemming from fire, windstorm, earthquake, and other perils. Additionally, as compared to the normal occupancy and use of completed projects, ongoing construction activities (e.g., welding, testing, demolition, storage) often increase the risk of loss.[9]

It is important to note that in contrast to Commercial General Liability (CGL) coverage (discussed below), there is wide variation in Builders' Risk policy language. Numerous insurers publish different forms, and no two policy forms are alike. Indeed, some insurance companies actually publish several different builders' risk policy forms. Because Builders' Risk insurance policies are non-standardized, it is imperative for the owner to pay particular attention to the coverage provisions to ensure that the owner remains adequately protected.

Finally, the verb "builder" in Builder's Risk is particularly apropos. Builders' Risk policies, unsurprisingly, terminate once the structure is complete. Once construction is completed, the policy terminates, and the owner must seek coverage through a CGL policy.

[9] James H. Costner, *Contract Requirements and Builders Risk Coverage*, 27 THE RISK REPORT 1 (1995).

### *B. A Cautionary Tale*

In *Liberty Insurance v. Weitz,*[10] Arizona State University learned first-hand the importance of clearly understanding the provisions contained in a Builders' Risk policy, and also learned how fickle these policies can be.

The facts of *Liberty Insurance* were undisputed. Weitz had contracted with Arizona State University ("ASU") to build dorms on the ASU campus. Unfortunately, a fire destroyed one of the dormitories while it was under construction. ASU assumed that destruction by fire was a covered peril under the Liberty Insurance's Builder's risk policy and sought indemnity under the policy.

Although fire damage was clearly covered under the policy, the policy also contained a warranty endorsement related to supervisory oversight. Liberty Insurance argued that ASU failed to adequately supervise the project and denied coverage.

ASU filed suit arguing that the supervisory warranty endorsement violated public policy and that the endorsement should not be enforced. ASU argued that because supervisory oversight warranties violate Arizona public policy in the CGL arena, the endorsement should be invalidated as applied to Builders' Risk policies.

The Arizona Supreme Court, however, disagreed with ASU and noted the distinctions between CGL and Builders' Risk policies. The court acknowledged that the adequate supervision endorsement would violate public policy if it were contained in a standard CGL policy. However, the court indicated that Builders' Risk policies are fundamentally different from CGL policies. The court explained that Builders' Risk policies are unique and therefore the provisions of the policy must control. The court explained that the warranty endorsement was clear and

[10] 158 P.3d 209 (Ariz. 2007).

unambiguous. Because ASU failed to meet the oversight condition, Liberty Insurance could deny coverage.

### *C. Takeaways: Builders Risk Insurance*

It is imperative to reiterate two important points: (1) no two Builders' Risk policy forms are alike, and (2) courts will often strictly enforce the provisions in the Builders' Risk forms.

Without a standard Builders' Risk policy, the owner *must* fully understand the provisions and exclusions contained in the particular Builders' Risk form purchased by the owner. The owner should ensure that the policy covers the risks specified in the contract and ensure that the policy does not contain extraneous warranties and endorsements that could bar coverage.

Finally, the standard AIA and ConsensusDOCS forms contain specific Builders' Risk coverage requirements. Thus, it is important to review the contractual requirements specified in the contract and ensure that the policy adheres to the contract.

## V. COMMERCIAL GENERAL LIABILITY PROVISIONS

### *A. CGL: Not Just Another Acronym.*

Commercial general liability insurance (CGL) provides coverage for accidental damage to persons or property caused by the insured party. It is common practice in the construction industry for owners to require contractors to name them as additional insureds under their CGL policies. Likewise, contractors will often require their subcontractors to do the same. As some put it, "downstream" parties provide coverage to "upstream" parties.

The obligation to provide coverage usually arises by way of a contract provision requiring the "downstream" party to name an "upstream" party as an additional insured under its liability policy. Coverage is typically accomplished through the issuance of an additional

insured endorsement. The additional insured often does not receive the actual endorsement but is notified through a certificate of insurance that it has been extended this coverage.

CGL policies provide coverage for damages arising from both bodily injury or property damage, and define those terms to require that the injury result in some physical injury or damage. Economic losses and emotional distress damages, without a concurrent physical injury, are not usually covered by a CGL policy, nor are losses for the insured's poor performance of the work called for in the contract.

### *B. Cautionary Tales: CGLs and Owner TKOs.*

It is difficult to overemphasize the importance of policy language, which is why parties in the position to bargain – like owners – should actually pay attention to the type of CGL coverage they are getting and exercise some control over the coverage in the formation stages of a contractual relationship. The owner in *Liberty Mutual Fire Insurance Co. v. St. Paul Fire and Marine Insurance Co.*[11] learned about this the hard way with regard to CGL coverage. In that case, the owner and a contractor entered into two service contracts for the contractor's work to modernize and upgrade elevators in one of the owner's facilities. The contractor obtained a CGL insurance policy. An accident occurred at the owner's facility and, not surprisingly, a personal injury lawsuit followed.

In a lawsuit filed to determine whether the owner was covered under the contractor's CGL policy, the trial court ruled that the owner was <u>not</u> an "additional insured" under the CGL policy. As with most insurance coverage cases, the analysis was technical because the court was required to review and reconcile the CGL policy with the two service agreements between the owner and the subcontractor – which is something the owner presumably did not do but should have done prior to asking the contractor to sign the dotted lines.

[11] 842 N.E.2d 170 (Ill. Ct. App. 2005).

Regardless, the court's analysis honed in on several key provisions in the CGL and the service contracts: First, the court highlighted the additional insured endorsement in the contractor's policy, which stated that an "insured" party included "any person, organization, state or other political subdivision, trustee or estate for whom you have agreed in writing to provide liability insurance." Second, the court examined the insurance provision in the service contracts between the owner and contractor, which stated:

> It is expressly understood and agreed by and between the parties hereto that no Work of any kind is authorized nor shall any Work be begun under this Contract until the Contractor shall have provided and delivered to the Owner satisfactory and acceptable evidence of insurance which is in full compliance with the Insurance Specifications attached hereto and incorporated by reference herein.

Third and finally, the court noted the insurance specifications in the service contracts, which provided that the contractor "will secure, maintain and provide evidence" of "General Liability insurance for all claims for personal injury, bodily injury, including death, and property damage which may arise from the operations under this contract."

Even though written contracts between the owner and contractor did in fact exist, it was not enough to provide coverage under the CGL policy when reconciling the provisions set out above. Thus, on appeal, the court affirmed the trial court's ruling that the contractor's CGL policy did not cover the owner, finding that the insurance provision only required the contractor to secure insurance to cover its *own* negligence.[12] The appellate court went on to state that "there was no language in the insurance provision or insurance specifications section that obligated [the contractor] to add [the owner] as an additional insured on the CGL policy."

In yet another story of the CGL policy not doing what the owner probably expected it to do, *Boise Cascade Corp. v. Reliance National Indemnity Co.*[13], a paper mill owner sought

[12] *Id.* at 342-43.
[13] 129 F. Supp. 2d 41 (D. Me. 2001).

coverage as an additional insured under its contractor's CGL policy for settlement monies paid to one of the contractor's employees injured on the project. The additional insured endorsement provided coverage to the owner "but only with respect to liability arising out of the negligent acts or omissions of the Named Insured." This language was construed by the court to limit coverage to liability arising out of the general contractor's negligence. It did not afford coverage to the owner for its own negligence.[14]

In both of these cases, the CGL policy was probably not the policy that the owners in these cases thought they were getting when they set forth the requirement of CGL coverage in their agreements with the general contractors. Lucky for the owners reading this article, though, they have the benefit of the advice contained herein, and can perhaps avoid the pitfalls of the owners in *Liberty Mutual Fire Insurance Co.* and *Boise Cascade Corp.*

### *C. Takeaways: CGL Policies*

Owners should never assume that a requirement for contractors to provide something that can be referred to by an acronym, like CGL policies, contain textbook language that is universally acceptable to all owners. Never should they passively sign off on agreements which may provide inadequate coverage. Owners must instead do three things: (1) Specify the coverage or policy form they prefer, (2) Ensure that its agreement with the contractor explicitly sets out the coverage they expect, and (3) Reconcile the owner-contractor agreement with the contractor's CGL policy to be sure that the policy does not fall short of the owner's requirements. At the very least, owners should make sure that they are considered "additional insureds", much unlike the owner in *Liberty Mutual Fire Insurance Co.*

Sitting "upstream," owners are generally in a position to call shots and should, without question, capitalize on the opportunity to get what they want and need with regard to CGL

[14] *Id.* at 48.

policies before coverage becomes critical. While no owner wants to think about all the bad things that could happen during or after a project, ignoring what could happen is a foolish and extremely risky approach. The subject is hyper-technical, but under no circumstances should an owners dismiss the importance of coverage pursuant to a CGL policy.

## VI. OWNERSHIP OF INSTRUMENTS OF SERVICES

### *A. What Are Instruments of Services, and Why Should I Care Who Owns Them?*

Instruments of Service are created by design professionals and include plans, specifications, drawings, opinions, reports, and calculations. They "belong" to the design professional that created them. Standard form AIA documents explicitly confirm this. The idea is to allow a design professional to use copyright law to exercise some degree of control over the use of its work and to protect the design professional's ability to get paid.[15]

Standard form AIA documents grant owners a limited <u>license</u> to use the documents created by the design professional. They do <u>not</u> grant ownership of the documents that the owner paid the design professional to create. Specifically, AIA B101-2007 establishes the following use and ownership scheme:

> (1) The Architect retains ownership of the Instruments of Service (including copyright) that the Architect creates.
> (2) Upon execution of the Agreement, the Owner receives a nonexclusive license to use and reproduce the Architect's Instruments of Service for certain permitted purposes including:
> --for construction purposes, including reproduction of the Instruments of Service by contractors, subcontractors, and suppliers for use in connection with the Work.
> --for submission or distribution to meet regulatory requirements including zoning approvals, and to obtain the building permit.
> --for use and maintenance of the Project.
> --for alterations and additions to the Project.
> (3) Continuation of the license is contingent upon compliance by the Owner with the Owner's contract obligations, including prompt payment of amounts due to the Architect.

[15] <u>www.irmi.com</u>

> (4) In the absence of prior written consent of the Architect (and the Architect's consultants), the license does not allow use of the Instruments of Service by the Owner in connection with other projects.
> (5) If the Architect rightfully terminates the Agreement for cause (i.e., the Owner is the party in default), the license is terminated.
> (6) If the Owner uses the Instruments of Service (e.g. in connection with alterations and/or additions to the Project) at some future point in time without retaining the Architect, the Owner:
> --releases the Architect from all claims arising out of such use.
> --agrees to indemnify and hold the Architect harmless from all costs and expenses (including defense costs) in connection with third party claims arising out of the Owner's use of the Instruments of Service; *provided, however,* that the indemnity does not apply if the Architect has been properly terminated for cause.

Under the default AIA terms, if the license granted by the design professional is terminated for any reason, then the documents can no longer be used for their intended purpose. Without access to design documents such as architectural or engineering documents, a project could be shut down altogether.

From an owner's perspective, AIA provisions relating to ownership of instruments of services should rarely go unmodified. The Maryland district court's decision in the cautionary tale below provides a shining example of why this is so.

### *B. A Cautionary Tale: A Story of How the Owner Became the Architect's Victim.*

Standing alone, the facts that led to a Maryland federal district court's decision in *Wereldhave USA-San Antonio, L.P. v. Peter Fillat Architects, Inc*[16] present a real-world example of standard form agreements "gone bad" – at least as far as the owner was concerned. (The architect in this story made off quite well.)

The owner in the recent *Wereldhave* case retained an architect to design a $400 million multiphase project. The architect provided five proposals for each part of the project it was hired to work on. Each of the proposals contained language that for each executed proposal, the parties would enter into a standard AIA agreement (B141). The AIA form agreements, as we

[16] 2010 WL 419388 (D.Md. January 29, 2010).

have described, included a provision granting the owner a nonexclusive license to use the architect plans, but further provided that the license would terminate if the agreement with the architect was terminated.

After the owner paid the architect nearly $2.7 million, the disputes between the two parties began. Eventually the disputes led to the owner's termination of the architect from part of the project, as well as an agreement that the owner would pay the architect an additional $150,000 in exchange for the construction drawings of that part of the project. Disputes between the parties continued, another year passed, and the owner terminated the architect from the entire project.

After being fired, the architect refused to allow the owner access to the construction drawings. With its hands tied, the owner filed suit in federal court in Maryland, seeking a temporary restraining order which would compel the architect to release the plans to the owner. Unfortunately for the owner, however, the federal court denied the owner relief. The owner did not get a restraining order, which would have given the owner prompt access to the architect's plans and an ability to proceed with the project.[17]

Given the recent date of the decision in this case, more than likely the owner and the architect remain at odds, and the owner is having to build significant litigation expenses into the cost of project as a whole. Had the owner on the front-end better dealt with the ownership of design plans and with the repercussions of termination of the architect, the owner may have avoided this litigation expense altogether.

### *C. Takeaways: Ownership of Instruments of Service*

Modern times have brought a whole new world of law known as intellectual property law which, as alluded above, applies to construction contracts and addresses the ownership of

[17] *Id.* at *4.

copyrights to such things as architect's design plans. It is a constantly changing, rapidly developing realm of law and, with its application to construction projects, adds another layer of nuances and concerns for owners, general contractors, and design professionals alike – all in addition to the headache of trying to know what's best for you under the equally-confusing implications of contracts and construction law.

Be acutely aware that just because you own a building does mean that you own the copyright to the building. Owners who fail to address copyright ownership or licensing in their agreements with design professionals sell themselves short. They may put themselves in a position of not being able to construct or complete a building, not being able to reuse building designs, or not being able to prevent others from using the designs they paid to have created.

Do not be held hostage by a design professional. At the very least, insist on modification of AIA form documents to provide that termination of an architect does not terminate the owner's license to use the architect's plans. Last but not least, consult experts to advise you on aspects of intellectual property law as it applies to construction and your projects. These are complicated areas of the law, worthy of their solid reputations as such.

## CONCLUSION

The risk shifting provisions profiled here require careful consideration, and savvy Owners don't miss the opportunity to improve their positions. This is unquestionably the case in the current U.S. construction economy, which has been truly on life support since the Fall of 2008. In 2010, only the most timid of Owners should accept standard form contract language.