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Risk Management Tools for the Design Professional



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Porous Piety: Unwritten "Contracts" Cost Far More Than the Paper They Aren't Written On

David A. Ericksen, Severson & Werson

Most people, and most professionals in particular, know what they should do. It is the stuff of aspirational New Year's Resolutions and Twelve Step Plans. Yet even those readily acknowledged "right principles" often fall to the wayside of neglect and outright avoidance. The mind and heart acknowledge and are willing, but the follow through falters. Nowhere is this more true for the world of design and construction professionals than in the arena of written/unwritten contracts. It may result from the enthusiasm to jump straight into the work, unresolved contract negotiations, or an attitude that the contract just isn't that important.

Nevertheless, almost universally, the annual insurance applications for architects, engineers, land surveyors, landscape architects, geologists, and construction managers proclaim a pattern and intent to secure a written agreement for each and every project – or at least almost every. Yet the claims against these same design and construction professionals frequently arise out of projects without a written agreement. In fact, for Liberty International Underwriters ("LIU"), more than 25% of all claims against small firms arise out of projects without a written agreement. That is multiples of the acknowledged projects without written contracts. That means that either those small firms are misrepresenting their contracting practices on their annual applications or there is a direct correlation between the lack of a written agreement and a resulting claim or litigation. Idealistically, the latter is the dominant issue. As will be discussed below, the lack of a written agreement creates a relationship and an environment which is far more prone to misunderstandings and claim vulnerability. Even worse, the same LIU data indicates that the severity of these claims in terms of expense and loss are also disproportionately greater.

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The clear implication is that there is more than theoretical value in a written agreement. Design professional service agreements can and should establish the four key “Rs”:

- Relationship
- Responsibilities
- Rights
- Rewards

Without a written contract, there is a relationship, but what that relationship “means” and the corresponding level of commitment is left open to differing, shifting and opportunistic interpretations. Similarly, the right to “rewards” (i.e. compensation) is also left open to good will and good faith ultimately predicated on the undefined perceived value of the services and deliverables prepared and received. If that were not enough by itself, the lack of a contract plants the seeds of potential disputes and misses the corresponding moments of risk and relationship management which can and should come through an agreement. Chief among those seeds of dispute and missed opportunities of education and consensus are the following:

Parties to the Relationship. Few design and construction projects are binary processes limited to two parties. Nearly all involve a cast of characters playing different roles. By contrast, contracts are generally limited to two or a few parties. Absent a clear written definition and commitment, the open question is often who is a party to the relationship with a corresponding right to assert claims and seek remedies based upon those services. The simple reality is that the list of potential claimants is far wider in the absence of a clear, written contract. It is the first (and simplest) benefit of reducing the relationship to writing.

Scope of Work: Defined and Limited. Simply stated, the scope of work is by far the most important portion of any contract. It defines and limits the services to be provided and the corresponding expectations. For those reasons, it should be as qualitatively and quantitatively detailed as is reasonable and also incorporate corresponding limitations and qualifications. Absent both the description and the limitations, the scope of work is effectively open-ended and undefined which can and does lead to disappointments and disagreements.

Professional Standard of Care. The common law and realistic standard for professional services is not perfection. However, many clients do not understand that and look to the degrees, licensing, and credentials of design and construction professionals to assert claims for any error, shortcoming, or disappointment. Without the benefit of a written agreement, such elevated and unrealistic expectations are often bolstered by marketing materials or proposals which seldom qualify themselves by reference to the prevailing standards of care.

While there are certainly other elements of a written service agreement which can and do foster claims, the four Rs identified above in conjunction with the three elements above dominate. At the same time, we live in a real world where written contracts do not always get consummated and sometimes it is even better to have no written contract than the onerous, one-sided document presented and insisted on by the client – sometimes even after work has begun or been completed. While the goal is and always should be a fair and detailed written agreement, the following three step approach for situations without a “final” written agreement can mitigate and overcome many of the dangers inherent in the lack of a written agreement and even facilitate the progress to an actual agreement.

Step One: The Written Scope of Work. As stated above, the written scope of work is the single most important portion of any agreement. That is true not just because it describes the services and processes, but also because it can incorporate provisions and language to address many of the key relationship, responsibility, and risk concerns. Chief among those opportunities are the following:

1. Limited. As stated above, one of the great dangers of the lack of a written agreement is that the scope of work is therefore inherently open-ended and ambiguous. A written scope of work or proposal can overcome much of that so long as it includes the appropriate limiting language. Such a clause would simply provide:

Consultant's services shall be limited to those expressly set forth above. Consultant shall have no other obligations or responsibilities for the Project except as agreed to in writing.

Alternatively or in addition, the scope of work may limit services through express exclusions of particular services or issues.

2. Standard of Care. The scope of work should be based on and limited to the professional standard of care. It is the natural place to say so. Such language could and should provide:

Consultant's services shall be provided consistent with and limited to the standard of care applicable to such services, which is that Consultant shall provide its services consistent with the professional skill and care ordinarily provided by consultants practicing in the same or similar locality under the same or similar circumstances.

This language is “standard”, except for the addition of the words “and limited to” which makes clear to the client that the standard of care is both the baseline and the extent of the obligation.

3. Relationship Boundaries. Any design and construction project should begin with appropriate client and project selection. It is fundamental to a positive and committed relationship. It is therefore critical to identify the parties to that

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relationship, disclaim others, and secure an ongoing commitment. To do so, there are really two key elements, both of which are readily appropriate for a proposal or scope of work.

The first is the identification of the intended parties and the disclaimer of others. Such language could provide:

Consultant's services are intended for the Client's sole use and benefit and solely for the Client's use on the Project and shall not create any third party rights. Except as agreed to in writing, Consultant's services and work product shall not be used or relied on by any other person or entity, or for any purpose following substantial completion of the Project.

The second may be partially repetitive, but reinforces the point that the agreement represents a mutual and affirmative commitment to a relationship which may not be transferred to others. Such language may provide:

The services and deliverables set forth in this Proposal may not be assigned or transferred without the written consent of both Parties.

4. Responsibility Boundaries. The disclaimer of third party rights may eliminate direct third party claims, but it does not eliminate shared liability with third parties or equitable indemnity claims based on principles of joint and several liability. To do so, design professional scopes of work and proposals should provide:

Consultant shall not be professionally, financially, or legally responsible for any person or entity not under its direct control and supervision.

5. Reliance Boundaries. The corresponding scope of work provision is then to declare a right to rely on information and work product provided by the client or others. Such language would provide:

Consultant may rely on information, documents, and services provided by Client and others except to the extent Consultant is actually aware of errors or omissions therein.

6. Assumptions. Finally, lists of exclusions and additional services are sometimes avoided as conveying the wrong message to clients. While such language may be particularly justified in a proposal or scope of work preceding an actual contract, an alternative approach to get across the same points and more is to establish a set of assumptions underlying the proposed scope of work. Lead-in language for such a section might provide:

Consultant's services are based on the following assumptions. In the event of any ultimate facts or events differ from such assumptions, Consultant's services, schedule, and compensation shall be adjusted accordingly

Step Two: Default Terms & Conditions

Affirmative communication of such a proposal with its underlying assumptions and limitations can greatly direct and contain the resulting relationship and claim exposure, even if there is ultimately no agreement. Even better is to attach a set of standard, but limited, terms and conditions which are expressly declared to control the commitments in the proposed scope of work until such time as there is a formal written agreement. Such standard terms and conditions could include the six provisions set forth above as well as provisions for payment, ownership of documents, and termination.

Step Three: Notice to Proceed

Finally, the post-claim narratives in situations without a formal written agreement predominantly sound of themes of “we always meant to complete the contract, but never got around to it.” To couple a proposed scope of work and default set of terms and conditions as described above with a corresponding “Notice to Proceed” or “Authorization to Proceed” signed by the client would effectively make it a binding agreement pending a subsequent document. That affirmation would then open it up to become not just a limitation on responsibility and claim exposure, but also an affirmative tool for collection of fees, limitations of liability, and dispute resolution. It also provides a powerful incentive and more balanced negotiation table for the ultimate consummation of a final written agreement.

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SmartRisk Checklist Can Help Your Firm Shore Up Cybersecurity



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