## Privity of Headache:
## Contracting Among The Design Team

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Much has been written on the proper considerations for an a/e contract. Articles and loss prevention guides contain numerous provisions and suggestions, so that your client's lawyer can ignore them and put together his own form. Even with the best contracts and intentions, a/e's frequently forget the rest of the team. Contractual liability, though, is like a bullet, passing through each contracting party until it gets to the last in line - all in line are wounded as liability passes through them. To be fair to the entire team, the design professional must take contractual precautions so that its consultants remain responsible and insured for their respective errors, and that all avoid incurring liability for decisions made upstream and without their input.

Contracting among the design team is at least as important as contracting on behalf of the design team, but consultant agreements are usually an afterthought. Architects will spend months negotiating and documenting an owner/architect agreement and then sign one-page proposals with consultants. To be effective, consultants should be included in discussions before execution of the owner/architect agreement. In addition, the architect/consultant agreement must incorporate the architect's agreement with the owner, and consistently apportion responsibilities among the team.

*Owner contracts with architect, requiring binding arbitration and minimum insurance limits for the entire design team of $2,000,000. Architect retains separate consultants for m/e/p design, lighting and acoustics, by signing their respective letter proposals. The letter proposals say nothing about arbitration or insurance. Following construction, owner claims to have incurred $1,000,000 in additional cost as a result of defects in m/e/p and lighting design. The architectural design is not at fault, but the owner demands arbitration and the architect is required to notify his insurance carrier and satisfy a deductible. Owner proceeds to win an arbitration award for $1,000,000 based entirely on alleged engineer error. The engineers testify in the arbitration, but are not bound by its result. The architect sues each engineer, but the architect is required to satisfy the $1,000,000 judgment while litigation is still pending against the engineers. In addition, the engineers maintain only $250,000 limits in professional liability insurance.*

### Proclivities of Privity

Privity of contract generally refers to the relationship between two parties to a contract - the owner and architect are in privity of contract. At the risk of over-generalizing, for *many* claims in *most* states, parties can only sue along contract lines of privity. They cannot leapfrog over their respective positions outside the lines of privity.

In the typical Owner-Architect contract, where the architect contracts with an engineering consultant for mechanical, electrical and plumbing design, an m/e/p design error requires the owner to sue the architect,

and the architect to sue the engineer. The owner cannot directly sue the engineer (again -- many claims, most states). The architect may have done nothing wrong, but will literally be in the middle of litigation between his client and his consultant, while paying legal fees and reporting to his own insurance carrier.

What if the architect is required to arbitration with the owner, but not with his consultant? Or if the consultant has a contractual limitation of liability, but the architect does not? Even when a/e's use AIA or industry form documents, they forget about riders and changes made during contract negotiations. If a change was made to the architect's standard form agreement with the owner, care must be taken to carry that change through the consultants' agreements. Because liability passes through the architect, the architect must make certain that the engineer is prepared to take, or at least share, the headache. This is accomplished through consistency among the contracts, incorporation by reference and "flow down" of appropriate risk.

## A Checklist For Agreements Among The Design Team

Every contract and relationship is different, but here are a few of the major issues to be considered when preparing your design team agreements.

*Incorporation By Reference*: One does not have to rewrite the prime agreement to get its terms in place. Incorporation by reference is a legal doctrine that allows one to refer to another separate document and recite that its terms are included. The law looks to intent of the parties. As long as the language is clear that the parties intended to include those terms, they will be included. When you intend to incorporate another document by reference, saying so will usually suffice: "The terms and provisions of the Owner/Architect agreement are incorporated by reference in this Architect/Consultant Agreement."

*Flow Down Clauses*: Contractors have long known the contractual equivalent to a basic sanitary sewer principal - effluent flows down to the lowest level. Subcontracts always contain a provision along the following lines:

For its scope of work, Subcontractor assumes and owes to the Contractor all of the duties and obligations that Contractor assumes and owes to Owner. Contractor assumes and owes Subcontractor all of the duties and obligations that Owner assumes and owes to Contractor.

The AIA Architect-Consultant agreements contain a similar provision, referring to the consultant's scope as the defined term "This Part of the Project." (Standard Form of Agreement Between Architect and Consultant, AIA Document C141 and the abbreviated form C142, Article 1, and para. 2.2). These clauses are critical to the architect and contractor, so that responsibilities can be passed down where appropriate. It is also important to the consultant to allow responsibility of the owner to "flow up" through the architect. If the owner furnishes incorrect information concerning the existing building, for example, the consulting engineer can point to the source of the information - the architect - who can turn to the owner for the same claim. (See, for example, Standard Form of Agreement Between Architect and Consultant, AIA Document C141, Article 6). (Incidentally, there are reported court opinions that judicially recognize that effluent flows to the lowest level - send me a request by email and I will send you a copy of one such case).

*Timing and Conditions of Payment*: If the owner will pay the architect following certain submissions, it would be dangerous for the architect to agree to pay its consultants unconditionally. If lien waivers or

lender approvals are required before payments can be made, the same conditions should be included in any consultant agreements. Many contracts also contain provisions that require payment to the architect as a condition of any payments to the consultants, regardless of cause. These "pay when paid" and "pay if paid" provisions are enforceable to different degrees in different states. Whether you are an architect or consultant, you should consult a local attorney before proposing or agreeing to such terms.

*Insurance*: Many owner/architect agreements call for the architect to carry some minimum level of coverage, and to require any consultants to do the same. Smaller engineering firms may not carry the same limits or even sufficient limits to satisfy the requirements of the owner/architect agreement. Check with the consultants before promising the owner that the entire design team will carry certain minimum limits. Moreover, you should not assume that you can insure for your consultant's errors. An architect is insured for its own negligence, not for the negligence of others. Realistically, any claim for engineering error will also include a claim for failing to coordinate the design disciplines. Nevertheless, an uninsured consultant means that the buck stops with the architect.

*Arbitration and Mediation*: If the architect is required to arbitrate or mediate with the owner, the consultants should be required to participate and be bound by any arbitration proceeding. (See, for example, Standard Form of Agreement Between Architect and Consultant, AIA Doc. C141, para. 9.2.4). Otherwise, the owner can obtain an enforceable judgment against the architect, leaving the architect to separately arbitrate or litigate with the consultant before a different arbitrator, judge or juror. Separate proceedings present the risk of an inconsistent result - lose to the owner without the consultant's help, and lose trying to recover from the consultant when he presents a defense to the owner's claims.

*Copyrights*: Many owner/architect agreements contain assignments or licenses for the owner to use the drawings. Make certain that the consultant agreements are consistent and that the consultants will agree to those terms. If the owner/architect agreement promises away the drawings, but the consultant agreements retain their respective copyrights, the architect could be in breach of his consultant agreements before pencil hits paper.

*Limitation of Liability*: If an architect contracts for a complete design, including various engineering disciplines, the architect is on the hook for all of the liability arising from all of those disciplines. If any consultant's contract includes a limitation of liability, the architect is agreeing to absorb any excess exposure. Take, for example, an office building design with a deficient structural design. The architect/engineer contract called for a fee of $100,000, with all liability limited to the amount of the fee. After discovery of excessive beam deflection, bracing and reinforcing are installed at a cost of $250,000. The owner makes a claim for $250,000, but the engineer points to its limitation of liability and will only reimburse the first $100,000. Assuming that the limitation is enforceable in the applicable state, the architect is stuck paying the difference.

*Shop Drawing Review and Site Visits*: Don't forget to deal with responsibility for shop drawing review and site visits. Too many owners try to keep fees down by limiting construction phase services. Even when such services are included in an architect's basic services, too many architects try to save money by limiting such reviews by engineers. We have seen a great number of claims arise from architects' decisions concerning engineering design intent or failure to pass on shop drawings to the appropriate consultant. Timing is important too. If the architect's agreement calls for shop drawing turnaround in 3 days, make certain that such timing is realistic among all of the design disciplines.

Privity of headache results primarily from lack of attention to agreements among the design team. Consultants should be involved before the owner/contractor agreement is signed, and the consultant agreements should be consistent with the prime design agreement. Making these agreements consistent will fairly allocate risk among the team, without unfairly burdening any one member with the liabilities of others.

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