

# Lessons Learned from Recent Design Professional Litigation

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This briefing discusses lessons learned from several recent court decisions addressing design professional risk and liability.

## Indemnification

**Contractor under a guaranteed maximum price (GMP) contract, the contractor cannot make indemnification claim against engineer for inaccurate design documents that caused extra costs where not resulting from third-party claim**

A contractor was awarded a GMP contract for a Marriott Hotel in Washington, D.C. In preparing its GMP proposal, the contractor relied upon “Preliminary Design Documents” that had been prepared by an engineer working under contract directly to the project owner. After receiving the GMP contract award, the engineering firm entered into contract with the contractor to provide the balance of design services for the project.

After completing certain construction phases, the contractor stated it determined that designs it was using were flawed, and it had to make midstream corrections to comply with various code requirements, thereby incurring unexpected costs. The engineer filed a motion for summary judgment, which was granted by the court. The reason is that a suit based on contract indemnification clause could only seek damages if they resulted from third-party claims against the

contractor. The contractor could not recover its financial losses by using the indemnity clause to make first-party claims. *Hensel Phelps Construction v. Cooper Carry, Inc.*, 2016 WL 5415621 (U. S. District Ct., District of Columbia, 2016).

The indemnity ruling is quite instructive. Even though the indemnity clause did not, on its face, limit indemnity to damages caused by third-party claims, the court explained that it is the only basis to find liability under an indemnity clause, and that—for first-party claims—a contractor is expected to just make a normal breach of contract claim against the other party.

The court said, “If the court were to read the indemnification clause in the way [contractor] urges—to cover [contractor’s] damages, including [contractor’s] own liabilities for costs it incurred in fixing [engineer’s mistakes]—then it would be redundant.”

## Lesson learned:

Historically, indemnification was only for tort claims for property damage and bodily injury claims made against the indemnitee. Breach of contract claims and first-party claims by a project owner were not intended to fall within the context of indemnification. Over the years, we have seen indemnification clause language increasingly broadened to cover all claims, damages and losses incurred by the indemnitee that “arise out of” the indemnitor’s work or services. This creates an uninsurable liability that we attempt to correct by modifying such clauses so that the design professional does not indemnify against “claims” at all, but rather indemnifies the owner for damages “arising out of claims.” We have further endeavored to limit claims to “third-party claims.” But as will be seen from the Town of Newport decision below, the indemnity should further be limited to only “tort” claims. As a party to its contract with the design professional, the client does not need a contractual right to indemnity in order to assert its claims against its design professional.

## Indemnification: limit it to damages resulting from tort claims

A recent court decision requiring an engineer to indemnify and defend its client, a project owner, against a routine contractor claim is a wakeup call to further clamp down on indemnification language so that only those damages resulting from tort claims against the indemnitee based on the negligence of the design professional will be indemnified, and that there will be no duty whatsoever to defend such claims.

In *Penta Corporation v. Town of Newport v. AECOM Technical Services, Inc.*, No. 212-2015-CV-00-011 (Merrimack, New Hampshire Superior Court, 2016), the trial court held that the engineer owed its client, the town, a defense against a contractor suit that alleged the plans and specifications prepared by the engineer and provided by the town to the contractor for bidding and construction were defective. It was a routine breach of contract claim by the contractor against the project owner, but the court concluded the indemnification language in the engineer's agreement with the town was broad enough to obligate it to defend the town against the contractor's claim.

### A. Some questions to consider

When an indemnification clause includes an obligation to "defend," what exactly does that mean? If the defense is limited to claims arising out of the negligence of the indemnitor, does that mean a finding of negligence must be made and then the indemnitor will reimburse the indemnitee for its attorneys' fees? Or, does it create a distinct and broader duty, separate and apart from the indemnification obligation, that requires the indemnitor to defend a claim "on behalf of the indemnitee" as soon as the claim is made, even if there is never a determination of negligence? Finally, what constitutes a "claim" that must be defended? Does it include a run-of-the-mill change order request from a contractor that subsequently becomes a complaint in court against the owner?

### B. Duty to defend applied to all claims – not just tort claims

The court noted that the duty to defend applies to "claims," "litigation" and "suits" that are "asserted against" the town and related to the engineer's negligent contract performance.

Significantly, the court concluded, "This language anticipates unproven allegations, meaning the duty to defend would necessarily arise prior to any factual finding as to [the engineer's] negligence or breach." The court said, "If [the engineer's] duty to defend only required it to reimburse the Town for the cost of a defense following adjudication of [the engineer's] negligence or breach, then the Town would necessarily have to choose its own counsel, thus rendering the [choice of counsel language in the clause] meaningless."

### C. "Arising out of" is a very broad term

The engineer argued that the language of the clause reading "but only to the extent arising from" served as a strict limitation on the engineer's responsibility. The court rejected that argument stating, "The phrase 'arising out of' has been construed as a 'very broad, general and comprehensive term' meaning 'originating from or growing out of or flowing from.'" According to the court, the phrase "indicates intent 'to enter into a comprehensive risk allocation scheme.' 'Arising out of' does not mean that any losses or claims must have been caused by [the engineer's] negligence or breach. Nor does it necessarily require an action for negligence or breach. A claim merely has to involve an alleged negligent act or omission in the performance of the contract."

Thus, the court concluded the engineer's assertion that adding the words "to the extent" in front of "arising from" did not alter the broad intent of the words "arising from."

### Lesson learned:

Revising the indemnity clause to be limited to "third-party claims" may no longer be adequate to protect the indemnitor. A contractor change order claim against an owner might be considered a "third-party claim." The solution is to add the word "tort" so that indemnity is only for "third-party tort claims."

The indemnity obligations imposed on the designer by this court could have been avoided by deleting words such as "arising from" or "related to" and instead specifying that indemnity would apply only to damages "to the extent caused by" the negligence of the designer. Moreover, words could be added to state that the indemnity applies only to damages arising out of "third-party tort claims." This could effectively eliminate indemnity for run-of-the-mill contractor claims. Finally, designers should not agree to defend their clients. That is an uninsurable liability.

## Indemnification action only accrues for statute of limitation purposes on date indemnitee pays judgment or settlement

Where a subcontractor failed to honor its contractual indemnification obligations to defend and indemnify a swimming pool installation general contractor against claims arising out of the subcontractor's work, the general contractor (GC) entered into a settlement with plaintiff who had been injured when diving into the swimming pool several years after construction of the pool was completed. The GC and its insurance carrier sued the subcontractor to recover their settlement costs. In defending against the suit, the subcontractor moved for summary judgment, arguing that the statute of limitations for enforcing the indemnity agreement had lapsed. This was rejected by the court, which held that the statute, which was actually a statute of repose applicable to

patent defects in design and construction (four years for patent defects and 10 years for latent defects), was not applicable to bar an action for indemnity.

As found by the court, "A cause of action for breach of an express indemnity agreement (contractual indemnity) accrues when the indemnitor sustains the loss by paying the money sought to be indemnified from the indemnitee." The indemnity does not accrue for statute of limitations when the original accident occurs, but instead accrues when the tort defendant pays a judgment or settlement as to which he is entitled to indemnity. *Valley Crest Landscape Development v. Mission Pools of Escondido, Inc.*, 189 Cal. Rptr. 3d 259, 238 Cal. App.4th 468 (2015).

### Lesson learned:

This decision demonstrates an important point about indemnification clauses that some risk managers may be overlooking when they agree to contractual indemnification. Whereas a claim might otherwise be barred by a statute of limitations or statute of repose because it is based on a tort claim arising out of a construction project, an indemnity clause may create a wholly different cause of action that is not subject to the ordinary statutes of limitations and repose. As in this case, an indemnitee might settle a claim and bring a breach of contract action against the indemnitor for refusing to tender a defense and provide indemnification as required by the contractual indemnification clause.

## Code compliance and warranty claims against professionals

### Contractor sues engineer for breach of warranty of professional services

Pulte Homes sued the engineering firm that performed certain engineering and testing services for a building site on which it built a home. It alleged the home developed structural problems after construction due to deficiencies in the engineer's site work and testing. After resolving defects asserted by the homeowner through arbitration proceedings, Pulte filed suit against the engineer seeking to recover the damages it incurred with the homeowner.

The theories of recovery, in addition to a basic negligence count, included a count based on the right to indemnity arising from breach of express or implied warranties. Pulte alleged that "S&ME expressly or impliedly warranted to Pulte that all work performed by them would be performed in a careful, diligent and workmanlike manner, and that any materials and/or services designed, supplied or sold by them for use on the project would be merchantable and fit for their intended or specific purpose." In reviewing the contract language, the court agreed that it "includes language arguably

in the nature of an express warranty." *Pulte Home Corp. v. S&ME, Inc.*, 2013 WL 4875077 (U.S. District Court, South Carolina, 2013).

For a sample contract clause to disavow and avoid all warranties, read the comment at the conclusion of this briefing.

The engineer argued the state law does not permit a cause of action for breach of warranty against a service provider. It is true that the courts in South Carolina had previously held that attorneys could not be sued for breach of express warranty to obtain a specific result. But the court said that was not applicable here because the services at issue are not legal services. According to the court, "They are, instead, services relating to testing or preparation of land, tangible things. Thus, the services at issue here may be more like...those where a product or some tangible item is involved, such as... architectural plans or specifications."

The court denied the engineer's motion to dismiss the warranty claim. The matter will now go to a jury to determine whether the engineer breached an express warranty.

#### Lesson learned:

Review the design professional contract carefully for words like "fitness for intended purpose," "workmanlike," "assure," "ensure," "shall meet all codes" and similar wording that might be interpreted as a warranty or guarantee. Recommend replacing those words with standard of professional care language.

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## Code compliance and warranty claims against professionals (continued)

### Architect not liable for implied warranty of habitability

Problems developed at a condominium complex several years after construction because air and water infiltration was damaging interior flooring and finishes. The condominium association filed suit against a number of parties involved in the design and construction, alleging the parties had breached the implied warranty of habitability. The condo association attributed the air and water infiltration to latent defects in the design, materials and building construction that were not discovered until 2007.

The architect had completed the drawings in 2000 and, although not discussed in the appeals court's decision, the statute of limitations for filing a negligence (tort) claim against the architect had already run its course. The estimated cost of repairs exceeded \$4 million, and the association alleged the developer-seller, the original GC, and the successor GC were all either bankrupt or out of business, and thus incapable of satisfying a \$4 million award.

The trial court dismissed the claims against several of the parties, including the architect. The condo association appealed. The appeals court affirmed the dismissal of the claim against the architect, providing a comprehensive discussion of the warranty of habitability and its application to design professionals. Board of Managers of Park Point at Wheeling Condominium Ass'n v. Park Point at Wheeling, LLC, 2015 IL App (1st) 123452.

Turning to the issue of whether an architect could be held liable under the implied warranty of habitability, the court noted that Illinois and a number of other jurisdictions had already concluded that a design professional cannot be sued under an implied warranty theory for providing professional services. The court cited cases

in several other jurisdictions where courts have declined to find that design professionals impliedly warrant their work will be merchantable, fit for a particular purpose or fit for its intended use.

While such implied warranties are customary in the sale of goods (i.e., materials and equipment), most jurisdictions have rejected their application to professional services. Design professionals preparing drawings and specifications for construction projects are performing a professional service; they are not selling goods.

The appeals court pointed out the principle that an architect does not warrant or guarantee perfection in his or her plans and specifications is long standing. The appeals court summarized the case law into two principles. First, the implied warranty of habitability of construction is traditionally applied only to those who engage in the construction and sale of new homes. Second, design professionals perform their services pursuant to contracts that set out their obligations, and courts have consistently declined to heighten their express contractual obligations by implying a warranty of habitability of construction.

The appeals court specifically rejected the condo association's argument that design professionals and builders are similar because both are already subject to the implied obligation to perform their tasks in a "workmanlike" manner. Citing to Black's Law Dictionary, the court noted a workman is a person who is "employed in manual labor, skilled or unskilled." Thus the term "workmen" does not include professional persons such as design professionals, and design professionals are not obligated to perform their professional services in a workmanlike manner.

#### Lesson learned:

Design professionals should be careful not to agree to contract provisions that require them to perform their services in a "good and workmanlike manner." While the phrase is seemingly innocuous, a court could find that it imposes a higher standard than the professional standard of care.

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## Code compliance and warranty claims against professionals (continued)

### **Contractor not excused from violating building code even if home owner directs him to violate the code**

Where a homeowner directed its roofing contractor to perform work in a manner that violated the building code, the contractor was nevertheless liable for a per se violation of the code. The homeowner's waiver of the code requirements does not preclude the contractor's liability for violation. In this case, the code permitted no more than two layers of roofing on the building.

The trial court issued a jury instruction advising the jury that if they found the code violation was a result of the homeowner's instruction, they need not assess damages against the contractor. The appellate court reversed and held it was an error to give that instruction; because the jury found that the contractor violated the code, judgment must be granted to the homeowner. *Downey v. Chutehall Construction Co.*, 88 Mass. App. Ct. 795 (2016).

In analyzing what impact, if any, a client's instruction to violate the code would have on the contractor's obligation to comply with the code and liability for non-compliance, the appellate court stated that a statutory right may not be disclaimed if the waiver would

"do violence to the public policy underlying the legislative enactment." The purpose of the building code, according to the language of the statute, "is to insure public safety, health and welfare insofar as they are affected by building construction, through structural strength...and, in general, to secure safety to life and property from all hazards incidental to the design, construction, reconstruction, alteration, repair, demolition, removal, use or occupancy of buildings, structures or premises."

Based on this public policy, the court concluded that, "To permit a waiver by a homeowner of his or her right to compel a contractor to comply with the contractor's obligations under the building code would permit, even encourage, contractors, and perhaps consumers to waive provisions of the building code on an ad hoc basis, in the hope of saving money in the short-run, but endangering future homeowners, first responders and the public in general." In reviewing all the issues in this case, the court found that the "consumer's oral waiver of a building code requirement cannot defeat the contractor's liability for the violation."

#### **Lesson learned:**

The question of whether a contractor or design professional can be excused from code compliance by direction of its client is one that comes up more often than might be expected. It seems that clients may have a number of reasons (i.e., cost cutting) for not complying with all the details of the building code. As this decision makes clear, the professional contractor or designer who designs or constructs in violation of code requirements may find itself strictly liable for damages arising out of the work that violated the code, even though it did what the client told it to do. Therefore, beware of clients that suggest not all code is expected or required.

## Insurance

### **Settling suit without prior approval of insurance carrier caused Insured to forfeit coverage regardless of whether the carrier was harmed**

The “no-voluntary payments” condition of an insurance policy was violated by an insured subcontracting concrete company when it entered into a settlement with its prime contractor and paid damages for contractual liability for construction delays, as well as for an accident, without first notifying its insurance carrier and obtaining prior approval to settle the dispute. When the subcontractor subsequently sought indemnification from its insurance carrier to be reimbursed the amount it had paid in damages, the carrier denied coverage.

The issue of whether the coverage denial was appropriate was litigated and then appealed through several levels. The appellate court decision held that the subcontractor’s complaint against the carrier should have been dismissed on a motion for summary judgment without regard to whether the subcontractor might be able to demonstrate the carrier was not prejudiced or harmed by the unauthorized settlement. *Travelers Property Casualty Company v. Stresson Corporation*, 370 P.3d 140 (Colorado 2016).

The requirement that an insured contractor must provide notice of a claim as required by the terms and conditions of a policy is a “fundamental term of the contract,” and it is not necessary for a carrier to prove that it was prejudiced due to the failure of the claim to be reported timely. In fact, the court stated that “applying the notice-prejudice rule to excuse an insured’s non-compliance with such a contractual [policy] provision would essentially rewrite the insurance contract itself and effectively create coverage where none previously existed.”

The court explained that, “the ‘no-voluntary payments’ clause clearly excluded from coverage any payments voluntarily made or obligations voluntarily assume by the insured without consent,” and the insurance policy emphatically stated that any such obligations or payments would be made or assumed at the insured’s own cost rather than by the insurer.

#### **Lesson learned:**

This case demonstrates the dire consequences of failing to comply with the terms and conditions of an insurance policy, particularly when it comes to providing the carrier with timely notice of a claim, and when it comes to obtaining prior approval before doing anything that might compromise or settle the claim.

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## Site safety

### **Scaffolding collapse: engineer, architect and project owner not liable for injuries**

Summary judgment was granted and sustained on appeal for all defendants in this case where three employees of a contractor were injured when scaffolding failed under the weight of a concrete slab that was being poured. The laborers' suit against contractor was dismissed based on the protections of the workers' compensation statute. Their suit against the engineering and architectural firms involved in designing and observing the project were dismissed because they were not involved in actual supervision and control of the contractor's work. Citing the AIA B141 agreement, the court found the engineer "was not obligated to inspect the scaffolding to ensure that it was in compliance" with the plans and specifications.

The court noted the engineer that designed the scaffolding is not subject to liability because it created a design that was impossible to build and, rather than seeking clarification regarding that design, the contractor used its own design to "splice" supporting posts without the knowledge of the engineer. *McKean v. Yates Engineering Corp.*, 2015 WL 5118062 (Mississippi 2015).

The court said there was no authority to support the conclusion that either the architect or engineer had an absolute duty to inspect the scaffolding or formwork to ensure the engineer contractor followed his design. In fact, unless expressly required by contract, there would be only limited

circumstances in which an engineer has a duty to notify or warn workers or employees of the contractor or subcontractor of hazardous conditions on the construction site. Since there was no written contract between the contractor and the engineer that designed the scaffolding, there certainly was no express contractual requirement imposed on the engineer.

The court did not stop there in its analysis of the engineer's potential duty to the laborers. It considered the seven factors outside of contractual responsibility that may determine whether supervisory powers go beyond the provisions of the contract:

- (1) actual supervision and control of the work;
- (2) retention of the right to supervise and control;
- (3) constant participation in ongoing activities at the construction site;
- (4) supervision and coordination of subcontractors;
- (5) assumption of responsibilities for safety practices;
- (6) authority to issue change orders; and
- (7) the right to stop the work.

The court found no evidence that the engineer did anything to fall within any of those seven factors. According to the court, the engineer "unequivocally said that he did not visit the construction site to determine whether [the contractor] followed his design." He had only one initial visit and then a visit after the formwork collapsed.

#### **Lesson learned:**

A design professional should pay attention to the seven factors identified by the court so that it does not create safety responsibility that it would not have otherwise had under the terms of its contract. It is important to start with good contract language and then stay within the bounds of the contractually defined scope of services so as not to invite potential liability.

## Individual member of LLC has no personal liability for negligence

An individual who is a licensed contractor is not deemed a “professional” that owes an independent duty of care outside of the contractual obligations of the limited liability company (LLC) that signed a contract with a homeowner. Such an individual cannot be found personally liable for the defective work performed through the LLC. A trial court held the individual was liable to the homeowner for constructing a new home at an insufficient elevation to satisfy permit requirements concerning flood elevations.

The dispute was not over whether the homeowner could recover from the LLC, but whether she could also recover from the individual. She argued that the individual lost the protection afforded by an LLC because he was a professional with an independent duty to her and that he performed negligently, thereby causing her damage. The appellate

court reversed the judgment and held the facts did not support piercing the corporate veil. *Nunez v. Pinnacle Homes, LLC*, 2015 WL 5972529 (Louisiana 2015).

The four factors considered by the court in determining whether to hold a member of an LLC personally liable were the following:

“1) Whether a member’s conduct could be fairly characterized as a traditionally recognized tort; 2) whether a member’s conduct could be fairly characterized as a crime, for which a natural person, not a juridical person, could be held culpable; 3) whether the conduct at issue was required by, or was in furtherance of, a contract between the claimant and the LLC; and 4) whether the conduct at issue was done outside the member’s capacity as a member.”

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## Contractor suits against engineer acting on behalf of owner

### **Private engineering firm qualifies for governmental immunity when working as city engineer**

A private engineering firm, under contract to a city to act as the City Engineer, was entitled to have a negligence and nuisance suit against it dismissed based on official or governmental immunity that was extended to it as an agent of the city acting as a “public official” when designing a storm water drainage system.

Official immunity turns on the conduct at issue, whether the conduct is discretionary or ministerial, and, if discretionary, whether it was willful or malicious. The fact that the engineer had malpractice insurance as required by its contract did not deprive it or the city of the protective benefits of the

official immunity doctrine. *Kariniemi v. City of Rockford*, 882 N.W.2d 593 (Mn. 2016).

This decision once again demonstrates the power of governmental immunity, or official immunity, as it may be called. In some cases, the government entity is entitled to immunity directly, and then the engineer or contractor may be able to claim that as an agent of the city it gets to clothe itself with that same immunity when acting in its capacity as engineer for the government. If an engineer or contractor may be legally entitled to raise governmental immunity protection as a defense against third-party claims, a public owner should not deprive the firm of that defense.

### **Lesson learned:**

Beware that some contracts contain language requiring designers and contractors to waive any governmental immunity they might potentially be able to claim against third-party suits. Preserving that immunity can be a valuable defense tool.

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## Contractor suits against engineer acting on behalf of owner (Continued)

### **Contractor's tortious interference judgment against county engineer reversed because engineer acted within scope of contract**

A road contractor's claim for entitlement to compensation for installing double the amount of fill material than was estimated in the bidding documents by the county engineer was untimely filed after the contract was completed. When the engineer recommended that only a partial amount of the claim be paid, the contractor sued the county for breach of contract and the engineer for tortious interference with its contract. Before filing suit, the contractor failed to first submit a "pre-suit notice" as required by the state law when suing a governmental entity.

The trial court rejected motions to dismiss and a jury awarded judgment of almost \$200,000 against the engineer. On appeal, the court reversed the judgment against the engineer because (1) the engineer was entitled to interfere because it did so within the scope of its contract, providing advice to its client, and there was no showing that the engineer acted with malice and bad faith; and (2) the county engineer was entitled to the protections afforded a governmental employee, including the requirement that no suit could be brought against it without a pre-suit notice first being filed. *Springer v. Ausbern Construction Co., Inc.*, 2016 WL 4083981 (Mississippi 2016).

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## Contractor suits against engineer acting on behalf of owner (Continued)

### **Engineer liable for failing to provide appropriate request for information (RFI) responses to contractor**

Engineering firm designed site plans for a rain tank system to be buried under a parking lot for a new church sanctuary. As a contractor began the project, it inquired of the engineer via a RFI about concerns for the suitability of the tank's location, given the high water table, and included questions about installation and performance.

Without addressing the performance issues or re-evaluating the choice of the tank system in light of the contractor's concerns, the engineer referred to information in the manufacturer's drawings to assure the contractor their ground water concerns would not impact the functionality of the tank. A few months after installation, the tank collapsed under the parking lot.

In litigation that followed, the trial court found the engineer breached its professional standard of care by: (1) failing to conduct due diligence regarding the suitability of the tank, (2) incorporating a manufacturer's specifications into its own plan without verifying them; and (3) failing to respond to appropriate questions during construction.

The decision was affirmed on appeal. The court determined that the suit was timely filed because an action for the negligence of a design professional is an action for breach of contract and, therefore, governed by the statute of limitations applicable to contracts instead of the statute of limitations applicable to negligence actions. *William H. Gordon Associates, Inc. v. Heritage Fellowship*, 291 Va. 122 (2016).

#### **Lesson learned:**

This case demonstrates the importance of providing more than a cursory response to an RFI. When reviewing contracts, if the time limit established for responding to an RFI is too short or unrealistic, the contract should be revised so the design professional can take the amount of time and effort for the review as may be required by the standard of care.

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## Contractor suits against engineer acting on behalf of owner (Continued)

### Teaming agreement is unenforceable as a mere agreement to agree in the future

A Teaming Agreement subject to the law of State of Virginia has been declared unenforceable because it did not contain any requirement that the prime member of the team award subcontracts to the other team members. Additionally, it did not contain contract sum or reasonable method for determining a sum. The Supreme Court of Virginia concluded that, "The rules of contract law do not apply to the Teaming Agreement because it is merely an agreement to agree to negotiate at a future date." *Navar, Inc. v. Federal Business Council*, 291 Va. 338 (2016).

Negotiations broke down over the division of the work through subcontracts, and the prime contractor failed to extend subcontracts to the team member.

The prime submitted a bid to the government without the subcontractors and was awarded the contract. The jilted subcontractor then filed suit, alleging breach of the teaming agreement. A jury found that the prime breached the teaming agreement and awarded the plaintiff's damages.

The appellate court threw out the jury decision and held that the teaming agreement did not result in any obligations of the prime contractor to its potential subcontractor since there was no subcontract document attached or incorporated into the teaming agreement that would have established the terms of the obligations of the parties to one another.

#### Lesson learned:

The lesson from this decision is that the parties need to pay attention to the state requirements when entering into teaming agreements to be certain they are enforceable.

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## Ownership and copyright of documents

### Project owner may lose right to use A/E's copyrighted documents due to failure to pay invoices

The question of what rights a project owner gets to the copyrighted plans and specifications prepared by its design professionals is one of critical importance that needs to be clearly addressed by contract. In *Eberhard Architect's v. Bogart Architecture, Inc. et al.*, 314 F.R.D. 567 (U.S. District Court, N.D Ohio), when a project owner failed to pay its architect, the architect terminated its contract for default and terminated the owner's nonexclusive license to use the architect's documents.

The owner and its new architect and contractors continued to use the documents over the protest of the architect. In response to the architect's suit, the defendants moved to dismiss the complaint based on the

argument that the contractor's payment requirement was a mere "covenant" upon which the architect could sue for damages, but was not a "condition precedent to the existence of the nonexclusive license."

The court concluded that this was indeed the law of the state, but it was the wrong argument to make in this case. That is because, although the nonexclusive license came into existence "upon execution" of the Agreement before payment was due, the contract expressly provided for "termination" of the license for subsequent non-payment." In other words, the parties agreed by contract that the license could be revoked. For this reason, the defendants' motion to dismiss was denied, and the matter will go to trial unless a settlement is reached.

#### Lesson learned:

Many project owners now seek to obtain copyright interest in the design professional's documents, or even state that the documents were prepared for the owner by the design professional that served as an employee for hire—and that the owner obtains exclusive rights to the copyright such that the design firm forfeits its own rights to the documents. If a designer is going to agree to give the owner either a license or copyright to the documents, the lesson from this court decision is that the designer can limit its client's rights by including contract language that states the license and copyright do not come into existence until payment is made (some states may permit that as a condition precedent) and that any license or copyright that has come into existence is automatically terminated for failure to make payment.

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