



## Understanding the Difference between Indemnification and Insurance

By Gail S. Kelley, P.E., Esq.

Indemnification clauses in design agreements are often considered to be “boilerplate” – something to be read quickly (if at all) after the parties have agreed on the scope of work and compensation. However, if a claim arises from the engineer’s services, an overly broad indemnification clause can create an uninsurable and potentially costly liability for the engineer.

The article *Understanding Indemnification Clauses* published in the January 2017 issue of *STRUCTURE* provided an overview of indemnification clauses. This article takes a closer look at indemnification clauses and compares indemnification with insurance. In many design agreements, the insurance and indemnification obligations are in the same section, which can create confusion. The agreement may further confuse the issue by requiring that the Indemnitees (the parties being indemnified) be listed as “additional insureds” on some of the engineer’s insurance policies. While both insurance and indemnification provide financial protection to the covered individuals, it is important to understand the difference between the obligations.

### Additional Insureds

The insurance obligations in a design agreement generally consist of the policies that the engineer is required to carry and the limits of each policy. The policies typically required are Commercial General Liability (CGL); Commercial Automobile Liability; Workers’ Compensation / Employers’ Liability, and Professional Liability Insurance (PLI). The agreement may also state that various entities must be named as additional insureds on certain policies. When an entity is an additional insured on another party’s insurance policy, it is covered by the policy under essentially the same terms as the Named Insured (the party that the policy was issued to), subject to any restrictions in the additional insured endorsement.

Often, an engineer will be required to name its Client and the Client’s lender (when the Client is the Owner) as additional insureds on its CGL policy. If a claim is filed against the Additional Insured for injury or property damage suffered by a third party, and

the injury or property damage was caused, at least in part, by the Named Insured, the Additional Insured will be covered under the policy, subject to the terms and limits of the policy and any restrictions in the endorsement. The Additional Insured is covered even if the Additional Insured’s negligence was primarily responsible for the claim.

However, most claims against an engineer will fall under its PLI, particularly if the engineer is not providing construction administration or doing work such as surveying or condition assessments which require the engineer to be on site. PLI policies do not allow additional insureds to be added to the policy; if the Client is performing design work or other professional services that could contribute to a negligence claim, it needs to be covered under its own PLI policy. Since the Client cannot file a claim directly under the engineer’s PLI, most design agreements require the engineer to indemnify its Client against claims caused by the engineer’s negligence.

Indemnification clauses are typically written such that they apply to claims arising under the engineer’s CGL insurance as well as its PLI policy. This provides additional protection to a Client who has been named as an additional insured on the engineer’s CGL policy. For example, if the engineer’s employee was injured while working on-site and filed a claim alleging that the Client was partially responsible, the Client could either file a claim under the engineer’s CGL insurance or seek indemnification from the engineer. However, the indemnification obligation is completely independent of the engineer’s insurance. In particular, naming the Client as an additional insured does not provide insurance against the indemnification clause. The extent of the protection provided to an additional insured is determined by the wording of the additional insured endorsement and the other terms of the insurance policy, not the wording of the indemnity clause.

### The Indemnification Obligation

The indemnification obligation is between the engineer and its Client; if the engineer



agrees to indemnify the Client for claims that are not covered by insurance, the engineer will be responsible for the claims itself. As an example, PLI only covers claims to the extent they are caused by the engineer’s negligence. If the engineer agrees to indemnify the Client for “all claims arising from its services,” it could be liable for the entire claim, even if the claim was partly caused by the Client or a third-party. The portion of the claim that was not caused by the engineer’s negligence would not be covered by PLI. Likewise, PLI does not cover defense of claims against indemnified parties; an indemnification clause that requires the engineer to defend claims arising from its professional services can expose the engineer to uninsurable risk.

An example of a well-written indemnification clause is the one in AIA C401, *Standard Form of Agreement Between Architect and Consultant*, which is often used when the structural engineer is providing its services as a subconsultant to the Architect.

§ 8.3 The Consultant shall indemnify and hold the Architect and the Architect’s officers and employees harmless from and against damages, losses and judgments arising from claims by third parties, including reasonable attorneys’ fees and expenses recoverable under applicable law, but only to the extent they are caused by the negligent acts or omissions of the Consultant, its employees and its consultants in the performance of professional services under this Agreement.

The indemnification clause in DBIA 540, *Standard Form of Agreement Between Design-Builder and Consultant*, can also be used as a model; however, two changes are recommended, as shown below. An “agent” can be almost anyone with a connection to the

Owner; many risk management consultants recommend not providing indemnification to such an ill-defined universe of entities. Also, attorneys' fees should be explicitly limited to those that are reasonable in terms of the claim.

10.2.1 Design Consultant, to the fullest extent permitted by law, shall indemnify and hold harmless Owner, DB and their officers, directors, and employees from and against losses, and damages including reasonable attorneys' fees and expenses, for bodily injury, sickness or death, and property damage or destruction (other than to the Work itself) to the extent resulting from the negligent acts or omissions of Design Consultant, anyone employed directly or indirectly by any of them or anyone for whose acts any of them may be liable.

It should be noted that, unlike the indemnification clause in the AIA C401, under the DBIA 540 the Indemnitee is entitled to attorneys' fees to the extent the claim resulted from the engineer's negligence, even if the fees are not recoverable under state law. Under the law in some states, a successful plaintiff in a negligence action is entitled to recover its attorneys' fees, but this is not true in all states. PLI generally will not cover attorneys' fees

unless they are recoverable under state law, but many clients will not accept the limitation that attorneys' fees are only indemnified to the extent recoverable under state law and will require language similar to that of the DBIA 540. Depending on state law and the terms of the engineer's PLI, this language can result in an uninsurable risk.

## A Caution for Contracts Governed by California Law

Under California law, an agreement to indemnify a claim arising from a design or construction project includes a duty to defend, unless there is an explicit disclaimer. If the project is in California or the parties have agreed that the design agreement will be governed by California law, the indemnification clauses cited above should be qualified by the addition of a sentence such as: "*The obligation to indemnify shall not extend to the defense of professional liability claims.*"

## Conclusion

Unfortunately, indemnification clauses are often extremely long and difficult to understand. Nevertheless, the wording of

the indemnification clause in every design agreement should be examined closely to determine whether the indemnification obligations will be covered by insurance. If the Client insists on wording that will result in uninsurable risks, the engineer should consider requiring that there be a limitation on its liability. ■

*Gail S. Kelley is a LEED AP as well as a professional engineer and licensed attorney in Maryland and the District of Columbia. Her practice focuses on reviewing and negotiating design agreements for architects and engineers. She is the author of Construction Law: An Introduction for Engineers, Architects, and Contractors, published by Wiley & Sons. Ms. Kelley can be reached at [Gail.Kelley.Esq@gmail.com](mailto:Gail.Kelley.Esq@gmail.com).*

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