SUBJECT: Prohibiting duty to defend provisions in certain governmental contracts

COMMITTEE: Licensing and Administrative Procedures — favorable, without amendment

VOTE: 6 ayes — Smith, Gutierrez, Goldman, Kuempel, Miles, D. Miller

0 nays

3 absent — Geren, Guillen, S. Thompson

WITNESSES: For — Gregg Bundschuh, American Council of Engineering Companies Texas; Bob Jones; (*Registered, but did not testify*: Michael Chatron, AGC Texas Building Branch; Brandi Bird, Burns and McDonnell; Douglas Varner, CDM Smith; Eric Woomer, Structural Engineers Association of Texas; Cathy Dewitt, Texas Association of Business; David Lancaster, Texas Society of Architects; Jennifer Mcewan, Texas Society of Professional Engineers)

Against — Barbara Armstrong, Harris County; Michael Pichinson, Texas Association of Counties; John Dahill, Texas Conference of Urban Counties; Scott Houston, Texas Municipal League; (*Registered, but did not testify*: Tom Tagliabue, City of Corpus Christi; Jim Allison, County Judges and Commissioners Association of Texas; Donna Warndof, Harris County; Mark Mendez, Tarrant County Commissioners Court)

On — (*Registered, but did not testify*: Perry Fowler, Texas Water Infrastructure Network)

BACKGROUND: Local Government Code, sec. 271.904 prohibits contracts for engineering or architectural services involving a governmental entity from containing certain provisions. The contract cannot contain a provision that requires the licensed engineer or registered architect to indemnify, hold harmless, or defend the governmental agency against liability for damage. There is an exception when the liability involves damage caused by or resulting from an act of negligence, intentional tort, intellectual property

infringement, or failure to pay a subcontractor or supplier committed by the contractor.

DIGEST:

HB 2049 would prohibit certain provisions in contracts for engineering or architectural services involving a governmental entity and would require a specific standard of care to be included in those contracts.

The bill would specify to what extent a licensed engineer or registered architect (contractor) contracting with a governmental entity could agree to a provision requiring the contractor to indemnify the governmental entity. The contractor would be held liable for damage only to the extent that the damage was caused by an act of negligence, intentional tort, intellectual property infringement, or failure to pay a subcontractor or supplier by the contractor.

If a contract contained an indemnification provision as described above, the bill would prohibit it from requiring a duty to defend. The bill would allow a provision authorizing the governmental entity to seek reimbursement of reasonable attorney's fees after a final adjudication deciding that the contractor was liable due to an act of negligence, intentional tort, intellectual property, or failure to pay a subcontractor or supplier.

The bill would require a contract for engineering or architectural services involving a governmental entity to include the standard of care that the contractor's performance must meet. The contractor would be required to perform services:

- with the professional skill and care ordinarily provided by engineers or architects practicing in the same or similar locality and under the same or similar circumstances; and
- as expeditiously as was prudent considering the ordinary professional skill and care of an engineer or architect and the orderly progress of the project.

If a contract included a provision establishing a different standard of care

than the one described above, the provision would be void and unenforceable. The bill would change the title of Local Government Code, sec. 271.904 to reflect the changes contained in the bill.

The bill would take effect September 1, 2015, and would apply only to a contract for which a request for proposals or a request for qualifications was first published or distributed on or after that date.

SUPPORTERS SAY:

HB 2049 would correct a recent trend in certain governmental contracts and prevent contractors from taking on a duty that was uninsurable. The bill would promote fundamental fairness and good public policy by protecting contractors that do not have equal bargaining power with governmental entities. The contracts for engineering or architectural services usually are drafted by governmental entities, and contractors have little power to object to certain provisions, such as a duty to defend. Duties to defend are uninsurable under professional liability insurance policies and are a financial risk to contractors.

The bill would promote fair dealings in these contracts because often mistakes that cause litigation later in a project occurred during the planning stage, when governmental entities were most involved. Contractors would not be financially responsible for defending governmental entities against lawsuits until it was finally adjudicated that the contractor was liable.

The bill would address a recent trend, as duty to defend provisions have not historically appeared in these contracts. The bill would not be fixing a problem so much as protecting against potential issues for contractors. Because the bill essentially would maintain the status quo, it would not have a detrimental effect on various groups as suggested by opponents.

The bill would require these contracts to include a certain standard of care. This would protect the contractors from being held to a heightened standard of care that could be unreasonable in the industry, as well as uninsurable under professional liability insurance policies. It is common for standards of care to refer to the location of the contractor, but that

would not give an out-of-town contractor the excuse to perform sub-standard work because the standard would apply to the area of practice, not the contractor's home.

Under the bill, if the contract contained a heightened standard of care that was void, there still would be an applicable standard of care. The bill would require a standard of care in these contracts, and that would be the applicable standard if the heightened standard was unenforceable.

The bill would not specify whether governmental entities could recoup attorney's fees in the event of a settlement or mediation of litigation prior to a final adjudication. In these situations, the parties could negotiate an agreement apportioning attorney's fees.

OPPONENTS SAY:

HB 2049 could shift the burden to defend unfairly to governmental entities, which generally do not micromanage projects they have hired contractors to complete. Under current law, a duty to defend or indemnify only arises when there is a lawsuit for negligence, intentional tort, intellectual property infringement, or failure to pay a subcontractor or supplier. While there can be joint liability for an act of negligence, that is not the case for a failure to pay a subcontractor. This bill would force governmental entities to defend against those claims until a final adjudication revealed that it was the contractor's fault.

The bill could affect taxpayers and businesses because it could increase litigation costs for governmental entities and cause some to no longer offer contracts to private businesses but instead to shop in-house for engineers or architects. The bill also could burden governmental entities with micromanaging projects to ensure no liability did arise.

The bill could discourage cooperation among contractors and governmental entities in the event of a lawsuit because if it was shown that the contractor was at fault, they would be responsible for the attorney's fees. This could create more litigation among the contracting parties to sort out each party's liability and costs.

The bill would require an unreasonable standard of care in these contracts. It would specify that the contractor's performance should be compared to that of other contractors practicing in the same or similar locality. This would allow an out-of-town contractor to claim a lower standard of care as compared to the area where the project was located.

The bill also could create a loophole for the standard of care required. It would void a heightened standard of care, allowing no standard of care to apply. That would be a bad precedent to set.

The bill could limit unfairly governmental entities' ability to recoup attorney's fees from contractors. It would specify that governmental entities could seek reimbursement of attorney's fees only after a final adjudication of liability that showed a contractor was liable for negligence, intentional tort, intellectual property infringement, or the failure to pay a subcontractor or supplier. The bill would be silent about what would happen if the governmental entity settled or mediated the case before it was finally adjudicated. Since most lawsuits are resolved before final adjudication, this bill essentially would ensure that governmental entities could not seek reimbursement for attorney's fees from contractors.