



Summer 2013

Disaster recovery contracts: Managing the risks

J. Kent Holland
ConstructionRisk, LLC

Recent disasters like Hurricane Sandy and the Deepwater Horizon oil spill have presented contractors with many opportunities to provide services in the areas of response, recovery and removal and reconstruction activity. Many contractors and professional consultants have

extensive knowledge and experience in responding to unprecedented and complex pollution conditions that require immediate emergency action. The recent uptrend in natural and man-made disasters may also draw more firms into contracts to perform disaster response services.

This briefing will focus on contractor immunity potentially available under federal and state laws as well as practical risk management tips that

can assist in minimizing potential liability when negotiating contract language.

Immunity protection potentially available

Immunity under federal law

The unprecedented nature of environmental disasters coupled with emergency response efforts may lead to lawsuits alleging a firm's services were negligent because the outcomes were not 100 percent successful. Where statutory immunities apply, they generally serve to encourage responders

to maximize response efforts by immunizing responders from liability risks that could act as a deterrent to providing such services.

The nature of the disaster, the kind of response action that is involved, the contract signatories and the applicable statutes are all factors that determine which immunities may apply. This briefing focuses on statutes and immunities that might potentially have been applicable to work performed in response to an oilrig accident.

Under Section 311 of the Clean Water Act as amended by the Oil Pollution Act (OPA), responders taking action or rendering care, assistance or advice before or after an oil spill have limited liability. They are immune from federal liability for removal costs or damages. (Federal Clean Water Act, 33 U.S.C. 1321(c)(4)).

The immunity is limited

Responders must follow the procedures for taking action that are consistent with the National Contingency Plan or Presidential direction to assist in availing themselves of the immunity defense. This immunity protection must be affirmatively pleaded as a defense to a claim or suit. This immunity does not apply to responders who may be the party responsible for the spill, nor does it apply to any responder who is grossly negligent or engaged in willful misconduct. The scope of immunity does not apply to damages owed to a third party for personal injury or wrongful death.

Where statutory immunities apply, they generally serve to encourage responders to maximize response efforts by immunizing responders from liability risks that could act as a deterrent to providing such services.

Immunity under state law

The OPA does not preempt states from passing their own oil spill liability laws, leading many states to adopt some additional form of responder immunity. The available protections and limitations or requirements placed on attaining the protection will therefore differ from state to state.

The available protections and limitations or requirements placed on attaining the protection will therefore differ from state to state.

For example, the state of Louisiana expressly immunizes the responder from civil penalties in addition to removal costs and damages (La.R.S. 30:2466). Florida's responder immunity also suggests a broader scope as the statute expressly applies

to voluntary actions rendered to assist in the containment or removal of pollutants. This immunity applies to any civil damages and does not exclude wrongful death or personal injury from immunity (Title XXCII, Chap. 376, Sec. 376.09(4)). Neither Louisiana nor Florida law immunizes gross negligence or willful misconduct of the responder.

Mississippi and Alabama both track closely with [the Oil Pollution Act] in terms of immunizing the responder from liability for removal costs or damages resulting from actions or omissions in the rendering of care, assistance or advice consistent with the National Contingency Plan or otherwise directed by the state (Miss. Code Ann SEC 49-18-5); (Ala. Coe 5-332.2(c)).

In order to preserve its immunity, the contractor must ensure that its services will be performed in compliance with the National Contingency Plan and any local, state or federal direction; they must act in accordance with the responder practices implemented at the site of an oil spill by the federal and/or state on-site coordinator.

Immunity risk management tips

The federal OPA statute and many state-specific statutes immunize the responder from liability for removal actions and damages resulting from the responder's acts or omissions, including negligence. It is prudent for the responder not to assume liability in contractual liability clauses for claims and damages arising out of its own negligence or out of the actions of others. Assuming

such liability could waive the responder's successful assertion of the immunity defense on its behalf, potentially resulting in the responder having to pay liability the law would have allowed it to avoid.

It is prudent for the responder not to assume liability in contractual liability clauses for claims and damages arising out of its own negligence or out of the actions of others.

When responding to a disaster, it is important to determine whether a federal or state official or other on-site coordinator is directing the work and whether the immunity law will still be applicable if not. If there is a coordinator, follow the responder practices implemented as long as they are consistent with the National Contingency Plan or applicable state directive.

Contract language risk management tips

General risk management ideas

- Pay attention to the standard of care provisions to ensure that work must only be performed to the skill ordinarily provided by firms practicing in a similar locality under the same or comparable conditions.

Disclaim all express or implied warranties and guarantees with respect to such performance.

State that the contractor shall have no liability for damages caused by oil not stopped by the work or for natural resource damages not resulting from the contractor's willful misconduct.

- Require that the responsible party and/or client indemnify, defend and hold harmless the contractor from liability as a result of the incident or oil spill. Ideally, there should be no indemnity by the contractor to the client.

If an indemnification clause must be provided, it should specifically disclaim any duty to defend the client and be narrowly limited to indemnify the client only for damages finally determined to have been caused by the willful misconduct or gross negligence of the contractor. Doing so assists in ensuring consistency with federal and state immunity laws.

- Attempt to avoid provisions that require the contractor to indemnify the client or other third parties for violations of laws or regulations, unless those violations result from willful misconduct.

Due to the fast pace of conducting an emergency response, the contractor risks unintentional violations of the law or violations based on reasonable but erroneous interpretations of the legal requirements that may be reasonable at the time of rendering work but may be judged as such at a later date by a court.

- If possible, agree only to assist an appropriate governing authority in the application for necessary permits to perform work instead of taking the responsibility to secure such permits. This minimizes risk associated with work delays due to the untimely issuances of permits.

Include provisions to waive consequential damages that apply to the client that waive contractor's liability for any special or consequential damages suffered by the client as a result of services rendered.

- State that there are no third party beneficiaries under the contract.
- Include provisions to waive consequential damages that apply to the client that waive contractor's liability for any special or consequential damages suffered by the client

as a result of services rendered. Special or consequential damages can be defined in the contract to include loss of capital, product, use on any system, or other property, or any other indirect, special, or consequential damage that arises in contract, tort (negligence), warranty, or strict liability.

- Include provisions for the express limitation of liability to limit the contractor's liability to its client and anyone claiming through its client for any claims, losses, costs or damages to a specific dollar amount or the total compensation received by the contractor.
- Include waivers of express or implied warranties and guarantees of the services, potentially including the warranting of materials and equipment, depending on the scope of the contract and language used.
- The prime contractor is likely to incorporate the subcontractor into its prime contract through a "flow down provision" in the subcontract.

Diligently review the prime contract, especially the provisions addressing standard of care, warranties, legal compliance, indemnification, insurance and other clauses affecting allocation

of risk and assumption of liability. Such provisions could potentially be enforceable against the subcontractor by the flow down provision as if the provision exists in the subcontract.

A subcontractor can take exception to those provisions in the prime contract that allocate unreasonable risk to the subcontractor.

This ambiguous standard appears to give the state unlimited discretion to determine whether the services are "proper and satisfactory."

Examples from contracts for response actions

ConstructionRisk, LLC had the opportunity to review a number of contracts for contractors that were considering working for states and private parties in response to an oil spill. Example language from contracts and revisions that could be suggested are set forth below:

• **Responsibility for permits**

- **State's language:** "The Contractor shall immediately engage the Army Corps of Engineers to secure the necessary permitting is in place to install the elements pertinent to the scope of this Contract."
- **Problem:** This ambiguous language suggests that the Contractor must obtain the permits.
- **Suggested revision:** "The U.S. Army Corps of Engineers (USACE) is responsible for issuing permits necessary to install.... It is understood that the Contractor has no control over the timing of issuance of permits by the UDACE and shall not be responsible for any delays to the work that may be caused by untimely issuance of permits."

• **Standard of care**

- **State's language:** "The Contractor shall perform the services in a proper and satisfactory manner as determined by the Department."
- **Problem:** This ambiguous standard appears to give the state unlimited discretion to determine whether the services are "proper and satisfactory."
- **Suggested revision:** "The Contractor shall perform the services consistent with the professional skill and care ordinarily provided by firms practicing in the same or similar locality under the same or similar circumstances. Contractor expressly disclaims all express or implied warranties and guarantees with respect to the performance of the services and any results that may be obtained by such performance."

• **Independent contractor**

- **State's language:** "The Contractor shall perform as an independent contractor and not as an agent, representative, or employee of the Department. The Contractor has been determined to be a Vendor to the Department under the Contract."
- **Problem:** Although it is typical to include an "independent contractor" clause in contracts, it might potentially adversely impact the ability of the Contractor in this case to assert that it is in fact acting on behalf of the State and is entitled as a state contractor to the same sovereign immunity that might be available to the state against third party actions. That is particularly so in light of the language stating the contractor is merely a "Vendor" as opposed to a state contractor.
- **Suggested revision:** "The Contractor shall perform its work as an agent and

representative of the state and shall be entitled to any and all immunities the state would have against liability to the same extent the state would enjoy such immunities if it were performing the services itself."

- **Indemnification**

- State's language: "The Contractor shall save and hold harmless and indemnify the State, the Department, and the county against any and all liability, claims, judgments or costs of whatsoever kind and nature for injury to, or death of any person or person and for the loss or damage to any property resulting from the use, service, operation or performance of work under the terms of this Contract, resulting from any negligent act, or failure to act, by the Contractor, its subcontractor, or any of the employees, agents or representatives of the Contractor or subcontractor to the extent allowed by law."

- Problem: Grammatically, the placement of the comma between "negligent act," and the words "or failure to act" makes it appear that any and all failures to act will require the contractor to indemnify the government even if that failure is not negligent. Due to the difficult working conditions and the need for speed, it seems more appropriate that the government should indemnify the contractor rather than the other way around.

- Suggested revision: "The State and/or Responsible party shall indemnify, hold harmless and defend the Contractor against any and all liability, claims, judgments or costs of whatsoever kind and nature for injury to, or death of any person or persons and for the loss or damage to any property resulting from the use, service, operation or performance of work under the terms of this Contract, except to the extent caused by the sole negligence or willful misconduct of the Contractor."

- An alternative idea: "The State shall indemnify, hold harmless and defend the contractor against any claim, liability, damages, and losses

that are covered, or could reasonably be deemed to be covered, by the State responder immunity statute, except to the extent the damages are determined to have been caused by gross negligence or willful misconduct of the contractor."

- **Waiver of consequential damages**

- State's language: The language requires the contractor to indemnify its client for all damages including consequential damages.
- Problem: The consequential damages that might be claimed to arise out of the contractor's work, or allegedly defective work, could far exceed actual damages and far exceed the contractor's fee and available insurance.
- Suggested revision: "Notwithstanding anything in this Agreement to the Contrary, it is agreed that Contractor shall not be liable in any event for any special or consequential damages suffered by the State or any agency or department of the State, arising out of the services hereunder. Special or consequential damages as used herein shall include, but not be limited to, loss of capital, loss of product, loss of use on any system, or other property, or any other indirect, special or consequential damage, whether arising in contract, tort (including negligence), warranty or strict liability."

- **Limitation of liability**

- State's language: States are not offering to cap liability through the use of a limitation of liability clauses.
- Problem: Due to the extraordinary circumstances, and higher than ordinary risks to the public that might arise out of performance of a recovery contractor's services, the liability to the contractor could far exceed the risk that should reasonably be accepted by the contractor and that can reasonably be insured.
- Suggested revision: Add a clause such as the following:

"To the fullest extent permitted by law, the total liability, in the aggregate, of Consultant, Consultant's officers, directors, partners, employees, agents, and sub-consultants, to Client, and anyone claiming by, through or under Client for any claims, losses, costs or damages whatsoever arising out of, resulting from or in any way related to this Project or Agreement from any cause or causes, including but not limited to tort, negligence, professional errors and omissions, strict liability, breach of contract, or breach of warranty, shall not exceed the total compensation received by Consultant or \$_____, whichever is greater."

Due to the difficult working conditions and the need for speed, it seems more appropriate that the government should indemnify the contractor rather than the other way around.

The consequential damages that might be claimed to arise out of the contractor's work, or allegedly defective work, could far exceed actual damages and far exceed the contractor's fee and available insurance.

...the liability to the contractor could far exceed the risk that should reasonably be accepted by the contractor and that can reasonably be insured.

Subcontractor selection

A prime contractor planning to subcontract the work should diligently evaluate the quality/ability of the subcontractor to perform the services, asking questions such as the following:

- Who are they?
- What experience do they have?
- What prior experience does the subcontractor have working with the prime contractor?
- Do they have sufficient personnel who have been trained to perform such work?
- Do they have sufficient financial capabilities?

The subcontract should include clauses requiring the subcontractor to indemnify and hold harmless the prime contractor against any and all claims and liability to the extent that the prime contractor is required to provide that to its own client.

The subcontract should include clauses requiring the subcontractor to indemnify and hold harmless the prime contractor against any and all claims and liability to the extent that the prime contractor is required to provide that to its own client.

The prime contractor should also review the subcontractor's insurance. Things to consider include:

- Is the limit adequate?
- Are the appropriate entities listed as additional insured's on the general liability policies including the prime contractor and project owner?
- Are there exclusions in the policy that bar coverage for work performed under the contract?

Conclusion

Contractors engaged in disaster response work should avail themselves of the special protectors the various immunity statutes provide. Responsible

parties should be held accountable for the liability consequences flowing from the oil spill incident, not the responders. It is imperative that contractors employ informed and smart risk management strategies to help avoid contractual liability the law otherwise would have immunized or eliminated.

Work related to oil spill response and other disasters invites significant liability risk. In order to decrease this risk,

contractors should seek legal counsel and review and negotiate contracts to provide appropriate protections consistent with the applicable laws of the jurisdiction where the work is to be performed.

It is imperative that contractors employ informed and smart risk management strategies to help avoid contractual liability the law otherwise would have immunized or eliminated.

About the author

Kent Holland is a construction lawyer located in Tysons Corner, VA, with a national practice representing design professionals, contractors and project owners. He is principal of ConstructionRisk, LLC, providing insurance risk management services and construction risk management services, including, but not limited to, advice to insurance underwriters; guidance to those procuring insurance; change order and claim preparation, analysis and defense; contract preparation; contract review and contract negotiation. Mr. Holland is publisher of ConstructionRisk.com Report and can be reached at Kent@ConstructionRisk.com or at (703) 623-1932.

ConstructionRisk, LLC is not a subsidiary or affiliate of Zurich and use of their products and services are independent of, and not included within, Zurich's product or service. Zurich expressly disclaims any and all damages and other costs that may arise related to the use of or reliance upon the products, services, representations or warranties made by or on behalf of ConstructionRisk, LLC is.

* The information in this Bulletin was compiled by ConstructionRisk, LLC for informational purposes only. Zurich neither endorses nor rejects the recommendations of the discussion presented, does not guarantee the accuracy of this information or any results and further assume no liability in connection with this publication, including any information contained herein. Further, the comments contained in this newsletter are for general distribution and cannot apply to any single set of specific circumstances. If you have a legal issue to which you believe this article relates, we urge you to consult your own legal counsel.

This Bulletin is provided for informational purposes only. Please consult with qualified legal counsel to address your particular circumstances and needs. Zurich is not providing legal advice and assumes no liability concerning the information set forth above.

This is sent to you by Zurich North America Commercial Construction, a unit of Zurich in North America, located at 1400 American Lane, Schaumburg, IL 60196. If you do not wish to receive future copies of C&DR Briefings from us, we will delete your email address from our email distribution list within 10 days of receiving notification from you. For removal, please send a reply to construction@zurichna.com with your request for deletion. We will honor your request.

©2013 Zurich American Insurance Company

