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Contribution and indemnity in professional liability claims

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CONTRIBUTION AND INDEMNITY IN PROFESSIONAL LIABILITY CLAIMS

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October 21, 2015

In construction defect cases involving issues of professional liability, the general course is that anyone potentially involved in the project is often named in the claim, either by way of a direct claim or third party proceedings. One of the foremost considerations for anyone involved in handling construction based professional liability claims is whether there are potential bars or limits to the claim against the professional. Certain claims, whether brought as a direct claim or as a third party claim for contribution and indemnity, will be dismissed for disclosing no cause of action. The determination of which claims are permitted may relate to the procedural basis of the claim, the contractual relations between parties, or a combination of such factors.

This paper considers the potential bars to claims for contribution and indemnity in professional liability or similar large scale construction actions. In doing so, consideration is given to the defences of agency, mitigation and contractual provisions. Professional service contracts, such as those used by architects, engineers or other like professionals, often contain a limitation of liability clause that restrict the professional's potential liability to a maximum amount and/or potentially for a set time period in which a claim must be issued. Governing or "prime" contracts often also provide that the professional will not be responsible for the acts or omissions of the general contractor, subcontractors or other persons performing work on the project. These clauses limit or prevent a plaintiff from claiming against the professional. However, if a plaintiff claims against other potential concurrent tortfeasors, such as the contractor or subtrades, those parties often seek to claim for contribution from the professional. In these circumstances, the professional or holder of the prime contract may be entitled to rely on limitation provisions despite not having a contractual relationship with these other parties. Similarly, where a subtrade does work that is covered in the prime contract, he or she may be able to rely on a limitation clause in the prime contract, despite having no privity of contract.

This paper is non-exhaustive but should provide the reader with initial considerations of potential bars and defences to claims for contribution. Counsel and clients issuing or defending claims for contribution and indemnity against professionals must be cognizant about which claims will be considered proper and which claims may potentially be dismissed for disclosing no cause of action. Proper consideration of these issues is best done at the start of the litigation and, at the very least, well before contributing to a settlement of the claim. By taking this prudent approach early, a party or proposed party can assess their potential risk, develop defences that do not wade into the technical aspects of the underlying claim, and adopt an early and aggressive negotiation stance.

Agency Defences

The first consideration turns on the status of the professional and the relationship with the owner of the project. If the professional is the agent of the owner, so that the professional's activities are essentially those of the owner, another defendant cannot claim against the professional directly. Any error by the agent is attributed to the principal and this is a defence against principal/owner. By example, an architect is an agent of the owner in developing and communicating the design.

In *Adams v. Thompson, Berwick, Pratt & Partners* (1987), 15 B.C.L.R. (2d) 51 (C.A.) ("*Adams*"), the British Columbia Court of Appeal ("BCCA") established:

> …that a third party claim will not lie against another person with respect to an obligation belonging to the plaintiff which the defendant can raise directly against the plaintiff by way of defence. Where the only negligence alleged against the third party is attributable to the plaintiff, there is no need for third party proceedings since the defendant has his full remedy against the plaintiff. On the other hand, where the pleadings and the alleged facts raise the possibility of a claim against the third party for which the plaintiff may not be responsible, the third party claim should be allowed to stand.
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> [emphasis added]

In that case, the BCCA heard an appeal from an order striking a third party claim against the plaintiff's solicitors. The architect defendants alleged that the plaintiff owner had retained the third party solicitors to provide advice on the project and that negligent advice caused or contributed to the plaintiff's loss. The architects further alleged that the solicitors ought to have advised the plaintiffs to mitigate their losses and that this failure to advise resulted in greater damage. The third party solicitors brought a summary trial application seeking dismissal of the claim. The presiding chambers judge agreed with the solicitors and dismissed the third party claim. The architects appealed.

Madam Justice McLachlin of the BCCA (as she then was) dismissed the appeal, finding that it was well established law that where a plaintiff contracted with two separate parties and later sued one of them, the sued party could not claim against the non-sued entity for contribution and indemnity if the substance of that third party claim could properly be raised as a defence. In effect, Madam Justice McLachlin found that the owner's failure to mitigate due to inadequate legal advice is a defence to the claim.

This holding has since been judicially considered as the first and second branch of the Adams principle. The first branch, discussed above, is that the third party cannot be sued for negligence attributable to the plaintiff. The second branch arises when an agent goes beyond the scope of his agency relationship and incurs duties to other parties. By example, an engineer responsible for the design of a development's water system that agrees to design a portion of the development's electrical for the contractor may be found to have incurred independent duties to the contractor. This work would fall outside of the scope of services to the principal and, if problems later arose, would not be attributed to the principal.

Madam Justice McLachlin further considered whether allegations that a third party failed to assist the plaintiff to mitigate, stating:

> Another situation where a third party claim cannot be raised because the obligation is essentially that of the plaintiff is where the claim is one that the proposed third party should have advised or assisted the plaintiff to mitigate his damages. In that situation, like the situation of agency, third party proceedings are redundant because the defendant can obtain any relief to which he may be entitled by reduction of the plaintiff's claim if he makes out the defence of failure to mitigate.
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> [emphasis added]

The BCCA held that the claim that the solicitors should have advised the plaintiff to mitigate was not a proper third party claim. Madam Justice McLachlin found that at all material times, the solicitors had acted as the agent of the plaintiff and therefore, the plaintiff was responsible for any potential wrongdoing. The duty to mitigate was the plaintiff's alone, which the architects could rely on as a defence in the main claim. In arriving at this decision, Madam Justice McLachlin considered sections 1 and 4 of the *Negligence Act* (the "*Act*"). She noted that section 1 of the Act provides for apportionment of liability where fault against the plaintiff is alleged. By contrast, where a plaintiff is not at fault, section 4 of the *Act* provides for contribution and indemnity for those at fault. In an agency situation where liability is attributable to the agent, section 4 of the Act is not applicable as the plaintiff bears the fault of the agent.

In *Laider Holdings Ltd. v. Lindt & Sprungli (Canada) Ltd.*, 2012 BCCA 22 ("*Laider*"), the BCCA considered an appeal dismissing fourth party claims against the plaintiff's solicitors in a complex commercial leasing matter. The defendant was a chocolatier that had entered into a leasing agreement with the plaintiff property owner. Relations between the parties broke down and the plaintiff commenced legal proceedings. The defendant argued that the plaintiff had made misrepresentations about the potential for the defendant to use the commercial space for its retail operations. Both the plaintiff and the defendant added their agents used in the negotiations as third parties. The defendant's leasing agent subsequently sought to add the defendant's solicitors as a fourth party for failing to properly advise the chocolatier that the proposed use of the property did not meet the applicable zoning requirements. The solicitors resisted the application to be added as a fourth party and the chambers judge found in their favour.

On appeal, the leasing agent argued that the solicitors had acted outside the scope of an agent and that the *Adams* principle did not apply on this basis. The basis for this argument was that it was not plain and obvious that the solicitors' potential fault could be attributed to the defendant tenant. . Accordingly, the leasing agent argued that the claims for contribution and indemnity should be permitted. After considering the complex facts and Ontario cases on agency, the BCCA dismissed the appeal, noting at para 46:

> In the words of *Adams*, that was an obligation "belonging to" Lindt (Ed: the tenant), which can be raised by the defendant by way of defence, making third party proceedings unnecessary. Finally, I respectfully adopt the reasoning in *Davy Estate*, and conclude that <u>even if one were to assume that in some circumstances, a client might avoid the consequences of an agency relationship by proving that he or she had retained a reputable agent, a defendant would nevertheless have no basis for a claim against the solicitor under the *Negligence Act* of this province for what remains the client's failure to mitigate</u>.

Based on this recent Court of Appeal holding, it appears unlikely that in cases where the alleged misconduct occurs after damage has already started to occur, that a court will permit a procedural third party claim on the basis of an agent negligently performing its duties and/or if it relates to mitigation. However, if an agent can be shown to have gone beyond the scope of his agency relationship and incurred independent duties to other parties that are not attributable to the plaintiff, then a third party claim may be permitted, which is discussed further below.

The reasoning in *Laider* was more recently applied by the B.C. Supreme Court in *Sun Life Assurance Co. of Canada v. 482147 B.C. Ltd.*, 2013 BCSC 1187 ("*Sun Life*"). In *Sun Life*, the plaintiff purchased a shopping centre that was later determined to have a water ingress issue. The plaintiff sued the shopping centre's developers, consultants, suppliers and contractors for negligent design and construction of the shopping centre. Prior to the purchase of the shopping centre, the plaintiff had retained Morrison Hershfield Limited ("Morrison") to visually inspect the roof. Morrison had no other involvement with the building. The contractors third partied Morrison and alleged that it failed to warn the plaintiff about the risks associated with the design and construction of the shopping centre.

Morrison applied for summary dismissal on the basis that, (1) Morrison did not inspect the wall cladding system, and (2) that any possible negligence against Morrison could be raised as a defence against the plaintiff. Mr. Justice Butler held that the first issue could not be determined on a summary judgment motion as such a finding could constrain the trial judge and there was a potential of inconsistent factual findings. However, relying partially on the holdings in *Adams* and *Laider*, Mr. Justice Butler found in favour of dismissing the second issue of the third party claim and stated:

> **46** In the present case, the Three Defendants say that the actions of MH could not have been part of Sun Life's mitigation efforts because at the time the work was performed, Sun Life had not purchased the property and had suffered no loss. <u>In other words, the Three Defendants say that the alleged failure by MH to provide advice which would have given Sun Life the opportunity to avoid the loss altogether or to minimize the loss is different in principle from advice given to a plaintiff who has an obligation to mitigate</u>.
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> **47** I cannot accept that argument. In my view the various factors considered in *Laidar* result in the same conclusion in this case. Here, <u>the Third Party Notices do not raise events related to the "initial loss". The actions which form the basis of all of the claims in the main action are the actions of the developers, contractors, consultants and suppliers who were involved in the construction of the Shopping Centre. The initial loss - that is the alleged deficiencies in design and construction - was complete when Sun Life contracted with MH</u>. The Applicants had no involvement in the development, design or construction of the Shopping Centre. They came on the scene well after the events which resulted in the alleged damage which forms the substance of the claims raised in the main action. As in *Laidar*, the allegations against the Applicants do not disclose "events giving rise to the initial loss".

> **48** Further, the substance of the allegations in the Third Party Notices is an allegation that the Applicants failed to protect the interests of Sun Life. It is the same kind of allegation which was recently found to fall within the first branch of the *Adams* rule in *Laidar* and *Owners of Strata Plan BCS 2077 v. Polygon Glenlloyd Park Ltd*., 2012 BCSC 945.
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> **49** Further, and most significantly, the fault alleged against Sun Life in the Third Party Notices is precisely that it failed to protect itself. The Three Defendants allege that Sun Life failed to inspect the Shopping Centre adequately or at all, that it failed to retain competent consultants and that it failed to take steps to detect and repair defects. The allegations in the third party proceedings against the Applicants raise the same issue: MH should have warned about the risks associated with the design and construction of the Shopping Centre. There is no question that this allegation is similar to the allegations which were found to be unsustainable in a third party claim in *Laidar* and *Adams*. It is an allegation that Sun Life failed to protect itself. To quote the language in those cases, this is an obligation "belonging to" Sun Life. Accordingly, it can be raised in defence by the Three Defendants. Indeed, it already has been raised in defence, and there is no need for a third party proceeding.
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> [emphasis added]

On this basis, Mr. Justice Butler dismissed the third party claim, holding that an allegation that a third party failed to perform due diligence was analogous to a claim that a third party failed to advise a plaintiff to mitigate. In both circumstances, the obligation remained that of the plaintiff and the claim fell within the first branch of the *Adams* principle.

Stepping Outside of Agency?

An important consideration with respect to an agency defence is whether a party can properly be considered an agent and the extent of the agency. Barron's Law Dictionary defines an agent as follows:

> One who, by mutual consent, acts for the benefit of another; one authorized by a party to act on that party's behalf.

In order for a potential party to be effectively considered an agent, there must have been mutual consent between the parties or a meeting of minds to establish an agency relationship in which the agent could act on behalf of or for the other party. If the agent acts in a manner that goes beyond what it and the principal have mutually agreed to, then the agent may have gone beyond the bounds of agency.

On the basis of the holdings in *Laider*, *Adams* and *Sun Life*, one has to establish that the agent's actions went beyond that of the agency relationship to support a claim against the agent. Such a situation will be difficult to establish. If the underlying wrongdoing has already commenced prior to the agent's involvement, such as with failure to mitigate or due diligence issues, no claim will lie against the agent. Nonetheless, it is important to keep in mind this potential argument.

In order to effectively establish a claim against the plaintiff's agent, one will need to demonstrate that the agent's conduct was outside of or went beyond the agent's scope and that the conduct created an independent duty to another party. For example, if an architect retained by the owner for a high-rise project solely to design the main structure subsequently engaged in side work for one of the contractors in designing architectural elements of the interior of the building and that subsequent work was a cause of damage, this may be sufficient to establish an independent claim by the contractor. Another example would be a situation where a structural engineer engaged in inspection of a building for their client, but while doing the inspection, also engaged in designing a remediation for the building's original owner. This latter work would clearly fall outside of the scope of the engineer's services to the original client and would essentially create a new client relationship. While this type of situation is unlikely to occur, it is important to be mindful of these potential issues.

Privity of Contract Issue: The Potential to Limit or Completely Bar a Claim

In a claim against a design professional, it is important to review the governing contract to determine whether there are clauses that would either bar or significantly reduce the claim. The two most common clauses are monetary limitations of liability and temporal limitations that may trump the applicable *Limitations Act* and discoverability principles.

In both *Board of School Trustees et al v. Killick Metz Bowen Rose Architects and Planners et al*, 2007 BCSC 28 ("*Killick Metz*") and *College of New Caledonia v. Kraft Construction Company Ltd.*, 2007 BCSC 1408 ("*College of New Caledonia*"), the B.C. Supreme Court considered separate claims made by clients and co-defendant contractors and subcontractors against each project's respective architect.

Contractual provisions of the Architectural Institute of British Columbia's ("AIBC") standard form client/architect agreement were at issue in both decisions. The AIBC contract included both a limit on the amount of damages and a time limitation on claims. The wording read as follows:

> 3.9.1 In consideration of the premises and of provision of the services by the Architect to the Client under this agreement, the Client agrees that any and all claims which he has or hereafter may have against the Architect in any way arising out of or related to the Architect's duties and responsibilities pursuant to this agreement (hereinafter referred to in this Article 3.9 as "claims" or "claim"), whether such claims sound in contract or in tort, <u>shall be limited to the amount of $250,000.00 each claim and $500,000.00 for all claims during each period of coverage as provided by the Architect's professional liability insurance or indemnity against errors and omissions in effect at the date of execution of this agreement, including the deductible portion thereof, and to the extent only that such insurance or indemnity is available to the Architect to satisfy such claims</u>. The "Architect" in this paragraph includes officers, directors, architects, his employees, representatives and consultants.
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> …
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> 3.9.6 The Architect's liability for all claims of the Client arising out of this agreement shall absolutely cease to exist after a period of six (6) years from the date of:
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> a. Substantial Performance of the Work,
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> b. suspension or abandonment of the project,
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> c. termination of the Architect's services in this Agreement, or
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> d. commencement of the limitation period for claims prescribed by any statute of the province or territory of the Place of the Work
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> <u>whichever shall first occur, and following the expiration of such period, the Client shall have no claim whatsoever against the Architect</u>. The Architect's liability with respect to any claims arising out of this agreement shall be absolutely limited to direct damages arising out of the Architect's services rendered under this agreement, and the Architect shall bear no liability whatsoever for any consequential loss, injury or damage incurred by the Client, including but not limited to claims for loss of profits and loss of markets.
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> [emphasis added]

In *Killick Metz*, the plaintiff school board sued its architect for negligent design, inspection, supervision and renovation of a school. The school was substantially completed in 1996 and that autumn, ground water leaks were discovered. Repairs were undertaken in 1996 and again in 2001 by both the architect and contractor. In 2003, further water ingress was discovered and the school board subsequently issued its claim in 2005. The architects applied for summary dismissal of the claim on the basis that it was barred by a contractual time limit.

The claim in *College of New Caledonia* arose from an alleged failed roofing system that caused water damage. The plaintiff sued a number of parties involved in the construction, including the general contractor, the architect, the roofing contractor that installed the roofing system and the manufacturer of the roofing system. The architects sought to have the claim summarily dismissed as against themselves on the basis of Articles 3.9.1 and 3.9.6 of the AIBC contract.

In *Killick Metz*, Madam Justice Gray agreed that the claim could be dismissed without the need for a full trial. In doing so, she determined that Article 3.9.6 of the AIBC contract prevailed over the principle of discoverability, and stated:

> [74] In my opinion, the principle of discoverability ought to be considered in construing a contract. However, as distinct from construing statutes, <u>the court must take into account the principle of primacy of private ordering and the fact that parties to a contract allocate certain risks between them</u>. In this case, clause 3.9.3 provides that the Architect's liability to the School Board arising out of the contract "shall absolutely cease to exist" six years after the earlier of several dates. <u>One of those dates requires application of the *Limitation Act*, which includes a principle of discoverability in the postponement terms of s. 6. However, the parties agreed that the Architect's liability would end earlier if the date which was six years following other events, including Substantial Performance of the Work, occurred first</u>.
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> [75] The parties entered into a contract which required time to run from a fixed event, being Substantial Performance, which clearly occurs without regard to the School Board's knowledge. In cases where the wording of a time limitation permits time to run for example from when the "damages were sustained", as in *Peixeiro v. Haberman*, [1997] 3 S.C.R. 549, 151 D.L.R. (4th) 429, or after "the date on which the right to do so arose", as in *Nielsen v. Kamloops (City)*, [1984] 2 S.C.R. 2, 10 D.L.R. (4th) 641, the court must consider if enough has occurred to cause "damage" or give rise to a cause of action. <u>In contrast, the pivotal event in the Consulting contract is the date of Substantial Performance of the Work as set out in clauses 3.9.6 and 1</u>.8.

> [76] The reasons the parties would choose to enter into such a term are easy to understand. The parties allocated risks between them under the terms of the Consulting Contract, with each party agreeing to accept a particular risk. They could order their affairs accordingly, such as by securing appropriate insurance.
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> [emphasis added]

Madam Justice Gray found that the parties in *Killick Metz* had contractually agreed that any potential claims ceased to exist 6 years after substantial completion of the school. As such and on the basis of contractual interpretation, Madam Justice Gray summarily dismissed the plaintiff's claim.

In *College of New Caledonia*, Mr. Justice Parrett quoted and approved the above passage from *Killick Metz* as his complete consideration of the discoverability principle in relation to the contrary contractual provision. On the basis of Article 3.9.6, Justice Parrett found that the plaintiff's right to claim against its architect, Greenwell, was extinguished.

Both holdings confirm that a professional may ensure peace of mind by contracting for certain limitations and courts are willing to enforce such contractual terms. These limitations allow the professional to know when a potential claim against it had expired and allocate resources accordingly. However, if the applicable contractual provision was poorly drafted and ambiguous, such as with respect to the time frame or application, a court may find that the provision did not apply and allow a claim to proceed outside of the contractual time frame. As such, it is important for anyone reviewing these clauses to be live to potential arguments about ambiguity or application.

Do Contractual Limitations Apply to Third Party Claims

In *College of New Caledonia*, both the roofing contractor and the general contractor, issued third party claims against the architect.

The roofing contractor argued that the AIBC client/architect agreement could not extinguish a third party's statutory right of contribution and indemnity or the right to claim for declarations. In support of this position, the roofing contractor relied on cases where the plaintiff had settled with a third party, resulting in an end to the claim between the plaintiff and respective third party.

Mr. Justice Parrett ultimately disagreed with the roofing contractor. In doing so, he confirmed the longstanding holding from *Giffels Associates Ltd. v. Eastern Construction Company*, [1978] 2 S.C.R. 1346 ("*Giffels*"). In *Giffels*, the Supreme Court of Canada ("SCC") held that a contractual provision in the general contractor's contract with the plaintiff barred a claim for contribution and indemnity by the plaintiff's engineer. '

The claim in *Giffels* arose from a defective roof on the plaintiff's plant. The contractor and the plaintiff contracted that the roof was only guaranteed for one year. Thereafter, the plaintiff had no right to claim for damage against the contractor. The plaintiff's claim against the contractor had been extinguished by a contractual provision in the general contractor's contract prior to the underlying claim being issued and as such, the plaintiff did not claim against the engineer. The plaintiff's right to claim against the contractor had also been extinguished prior to the defendant engineer's third party claim against the contractor for contribution and indemnity being issued. The contractor applied for dismissal of the third party claim on the basis that the claim had been contractually extinguished. The trial judge disagreed, but both the Ontario Court of Appeal and the SCC subsequently held that the claim was barred.

The decision of the SCC was delivered by Laskin C.J. On behalf of the court, he stated:

> What we have here is a case where the immunity of Eastern from liability did not arise from some independent transaction or settlement made after an actionable breach of contract or duty, but rather it arose under the very instrument by which Eastern's relationship with the plaintiff was established. <u>Giffels (Ed: engineer) had no cross-contractual relationship with Eastern upon which to base a claim for contribution; and once it was clear, as it was here, that Eastern could not be held accountable to the plaintiff for the latter's loss, any ground upon which Giffels could seek to burden Eastern with a share of that loss disappeared.</u>
>
> [emphasis added]

The SCC held that since the Plaintiff was contractually barred from recovering from the third party, the defendant, who did not have a separate contractual relationship with the third party, was also barred from seeking to burden the third party with any portion of the plaintiff's loss. The decision in *Giffels* has oft been relied on for the proposition that if a party has a complete contractual bar from a claim by a plaintiff, then there is no right of contribution and indemnity for the other potential tortfeasors.

In *College of New Caledonia*, Mr. Justice Parrett relied on the holding in *Giffels* to dismiss the roofing contractors argument that the AIBC contract could not extinguish its right to a third party claim. He stated:

> **75** The decision in ***Prairie Hydraulic*** considered a situation in which the plaintiff had settled a claim with the third party and it did not consider the Supreme Court of Canada's decision in ***Giffels Associates Ltd. v. Eastern Construction Company***, [1978] 2 S.C.R. 1346 and ***Bow Valley Husky v. Saint John Shipbuilding***, [1997] 3 S.C.R. 1210.
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> **76** The significant difference between the issue in ***Prairie Hydraulic*** and that in ***Giffels*** can be found in the following passage from the decision of Chief Justice Laskin at p. 1355:
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>> What we have here is a case where the immunity of Eastern from liability did not arise from some independent transaction or settlement made after an actionable breach of contract or duty, but rather it arose under the very instrument by which Eastern's relationship with the plaintiff was established. Giffels had no cross-contractual relationship with Eastern upon which to base a claim for contribution; and once it was clear, as it was here, that Eastern could not be held accountable to the plaintiff for the latter's loss, any ground upon which Giffels could seek to burden Eastern with a share of that loss disappeared.
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> **77** Keith Panel also relies upon the Court of Appeal decision in ***British Columbia Ferry Corp. v. T&N plc***, [1995] B.C.J. No. 2116. In this appeal a series of third party notices which had been struck out were ordered reinstated essentially for procedural purposes.
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> **78** The original application followed a settlement between the plaintiff and the third parties.
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> **79** In my view neither this decision nor that in ***Rurka v. JLG Industries Inc***, [1999] B.C.J. No. 658, supports the proposition that Keith Panel may continue to seek declaratory relief where no liability or claim exists between the plaintiff and the Architects.
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> [emphasis added]

On the basis of the complete contractual bar that protected Greenwell from any claims by the plaintiff, Justice Parrett dismissed the roofing contractor's third party claim.

The general contractor argued that the expiration of a limitation period applicable to claims of the plaintiff against an immune concurrent tortfeasor could not release the immune tortfeasor of liability for contribution and indemnity to the other tortfeasors, including the general contractor, when the claim arose within the contractual limitation period but the main action stated after the limitation period expired. Again relying on *Giffels*, Justice Parrett disagreed, stating:

> **89** What Kraft seeks to do here is to ignore the reasoning in ***Giffels*** by asserting as a distinction the fact that the expiration of the limitation period occurred after the cause of action arose. <u>Even if this distinction has any substance, this interpretation amounts to a rewriting of the contract between the parties destroying the very substance of both clause 3.9.6 and 3.9.1 and eliminating the very limitations and protections bargained for by the parties</u>.
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> **90** Allowing a claim for purely declaratory relief to proceed is discretionary relief which must be exercised with the utmost caution. This is not a case where, in my view, that extraordinary remedy should be granted.
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> [emphasis added]

Mr. Justice Parrett then also applied the Adams principle and held that it was inappropriate to allow a claim for contribution and indemnity to continue where the substance of the claim could be used as a defence to the underlying claim.

In *British Columbia (Workers' Compensation Board) v. Neale Staniszkiz Doll Adams Architects*, 2004 BCSC 1629 ("*Neale*"), the Supreme Court of British Columbia found that sub-consultants could, in certain circumstances, benefit from the limitation of liability clause contained in the prime consultant's contract with the owner of a project. The limitation clause at issue was Article 3.9.1 of the AIBC contract, set out above (limitation on damages). The case arose with respect to structural deficiencies and determination of liability for said deficiencies. The owner sought to sue its architect, which it had contracted with, and to sue an engineer retained by the architect. The engineer had no contract with the plaintiff owner.

The Court in *Neale* applied the reasoning of the SCC in *London Drugs Ltd. v. Kuehne & Nagel International Ltd.*, [1992] 3 S.C.R. 299 ("*London Drugs*"). In *London Drugs*, the SCC held that, where a limitation of liability clause, either expressly or impliedly, extends its benefits to the employee seeking to rely upon it, and the employee performs the very services provided for in the contract between the employer and client, the employee will be protected.

Based upon this analysis, the court in *Neale* found that sub-consultants should be entitled to benefit from a limitation of liability clause found in a prime contract in circumstances where there is an express agreement to extend any limitation of liability to sub-consultants, or where it can be shown that sub-consultants' services were included in the scope of services specified in the prime contract. Specifically, the benefits of a limitation of liability clause may flow to a sub-consultant where:

1. the limitation of liability clause makes specific reference to the sub-consultants;

2. the prime consultant lists the sub-consultants it intends to engage; or

3. the owner is advised specifically of the services the sub-consultants will be providing in contemplation of the prime contract.

Mr. Justice Burnyeat further held that even if the parties do not expressly agree, a limitation of liability clause may be extended to the sub-consultants where the services provided by the prime consultant are actually carried out by employees or agents of that prime consultant, on the basis that no party who performs the very services required under the contract should be excluded from the benefit of the limitation of liability made available to the primary provider of the services. Therefore, where the prime consultant hires the subconsultant, as in a design build, the limitation seems to apply.

The court in *Neale* found that the parties to the contract expressly agreed to extend any limitation of liability to third party sub-consultants because:

1. the architect was required by the owner to identify in the "Other Conditions of Service" part of the agreement the sub-consultants to be engaged;

2. the sub-consultant in question was listed in the "other Conditions of Service" part of the agreement;

3. the owner was specifically advised that the sub-consultant would be one of the suppliers of services contemplated by the agreement; and

4. it was acknowledged in the agreement that the architect and its sub-consultants would not be required to contribute to the cost of project-specific insurance if they were already paying fixed annual premiums.

In *British Columbia v. R.B.O. Architecture Inc.,* 1995 CanLII 945 (BCSC), the court came to an opposite conclusion on very similar facts. In that case, the defendant, R.B.O., was hired to design an apartment building for persons with disabilities. The head contract included a limitation of liability clause that limited liability to $250,000 per claim and to $500,000 for all claims during each policy period. R.B.O. hired an engineer, P.J.B., as a sub-consultant. Among the issues raised on summary trial were whether or not P.J.B. could rely on the benefit of the limitation of liability clause in the head contract and whether the plaintiffs were entitled to costs of their action in addition to the amount provided in the limitation of liability clause.

The court found that, while P.J.B. was certainly acting in the course of its employment when the facts giving rise to the claim arose, the limitation of liability clause in the contract in question was not expressly or impliedly extended to P.J.B. P.J.B was not entitled to rely on the limitation of liability in the head contract. It found that because the contract specifically mentioned the architect in the limitation of liability clause, only the architect's liability could be limited. The court distinguished this kind of contract from the kind of contract found in *London Drugs*, *supra*. It found that this contract was part of a "more complex contractual scheme" in which "the personal relationship between the contracting parties [was] an important factor in the contractual relationship" (at paragraphs 107 and 108).

If the sub-consultants are able to rely on a limitation clause, in the absence of project-specific professional liability coverage, the applicable limitation of liability may be the insurance "available" to the prime consultant under its own professional liability insurance policy. If the aggregate limit has been reduced, liability will likewise be reduced.

The *Neale* decision considers this issue to some extent. In *Neale*, the limitation of liability clause was initially worded as clause 3.9.1 of the AIBC contract, quoted above from *College of New Caledonia* and *Killick Metz*:

The clause specifically links the architect's limits of liability to the amount of professional liability insurance it is entitled to. At the request of the owner, the clause was amended to remove the limitation to $250,000.00 each claim and $500,000.00 for all claims. It was replaced with the following clause:

> The insurance coverage per claim and for all claims will be as determined by the Client and as stipulated in a project specific professional liability insurance policy to be obtained by the Client. The Architect and its subconsultants will contribute to the premium cost of such policy to the extent of the premiums that would have been payable by them with respect to the project under their respective general practice policies. No contribution to the premium cost will be required if the Architect or its subconsultants pay fixed annual premiums to Encon Insurance Managers Inc.
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> …

> for all claims during each period of coverage as provided by the Architect's professional liability insurance or indemnity against errors or omissions in effect at the date of execution of this agreement, including the deductible portion thereof, such limitation shall apply to the extent only that such insurance or indemnity is available to the Architect to satisfy such claims.

In *Neale*, the limitation of liability of the architect and sub-consultants was clearly linked to the amount of available insurance. The owner failed to obtain the project specific professional liability insurance policy and argued that because there was no policy in place, the architect's liability was unlimited. The architect and the sub-consultants argued that it was the owner's fault that no insurance was in place and therefore their liability should be limited to zero. The court found that the architect's and the sub-consultant's liability was limited to the amount of coverage the architect had pursuant to its own professional liability policy, which was $1,000,000.00. The judgment did not specifically state whether the sub-consultant's liability was jointly limited to $1,000,000.00. In fact, the judgment did not address the sub-consultant's limitation of liability at all, although the issue was before the judge.

Potential Partial Contractual Bars

In *PDC 3 Limited Partnership v. Bregman + Hamann Architects et al.* (2000), 49 O.R. (3d) 722 (ONSC), ("*PDC*"), the Ontario Superior Court of Justice heard a Rule 21 motion to determine (1), whether a monetary contractual limitation clause in the sum of $250,000 between the plaintiff and the architect limited the co-defendants' claim for contribution from the architect to that amount, and (2) whether the existence of that clause reduced the amount that the plaintiff could recover from the other defendants.

Ontario Superior Court of Justice Decision

Justice Chapnik initially noted the decision in *Giffels* was authority for the fact that a co-defendant was not permitted to claim contribution and indemnity, pursuant to the relevant Negligence Act, where there was a contractual provision completely excluding liability. However, he noted that the Supreme Court had not turned its mind to whether a monetary limitation clause would also limit the amount of the claim of the co-defendant. Justice Chapnik further noted that Lambert J.A. in *London Drugs Ltd. v. Kuehne & Nagel International Lt*d. (1990), 45 B.C.L.R. (2d) 1 (B.C.C.A.) at p. 58 had found that the holding in *Giffels* only applied where one of the tortfeasors had a complete defence. Justice Chapnik noted that this portion of the decision was not considered by the Supreme Court of Canada (*London Drugs Ltd. v. Kuehne & Nagel International Ltd.*, [1992] 3 S.C.R. 299).

At paras 25-27 of *PDC*, Justice Chapnik stated:

> [25] As already indicated, Lambert J.A. held that the decision in Giffels only applies where there is a complete defence available to one of the tortfeasors, which was not the case here. The Supreme Court of Canada in London Drugs Ltd. v. Kuehne & Nagel International Ltd., [1992] 3 S.C.R. 299, 97 D.L.R. (4th) 261, upheld the decision of the British Columbia Court of Appeal without comment on Lambert J.A.'s view of the applicability of Giffels to claims for contribution in the context of limitation of liability clauses. Iacobucci J. for the majority, held, at p. 448, that the rule of privity should be relaxed to allow employees to benefit from a limitation of liability clause between their employer and a customer, if the clause expressly or impliedly extends its benefits to the employees, and if the employees were acting in the course of their employment and performing the very services provided for in the contract when the loss occurred.
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> [26] Without referring to the issue of contribution as between the employees and the employer, Iacobucci J. simply viewed it as "absurd" to allow the customer, by suing the employees in tort, to "circumvent or escape a contractual exclusion or limitation of liability" in the name of privity of contract (at pp. 444-45). Commenting on the equities, Iacobucci J. said, at p. 446:
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>> According to modern commercial practice an employer . . .performs its contractual obligations with a party. . . through its employees. As far as the contractual obligations are concerned, there is an identity of interest between the employer and the employees. It simply does not make commercial sense to hold that the term "warehouseman" was not intended to cover the respondent employees and as a result to deny them the benefit of the limitation of liability clause for a loss which occurred during the performance of the very services contracted for. Holding the employees liable in these circumstances could lead to serious injustice. . . . Such a result also creates uncertainty and requires excessive expenditures on insurance in that it defeats the allocations of risk specifically made by the contracting parties and the reasonable expectations of everyone involved . . . the doctrine of privity should not stand in the way of commercial reality and justice. Clearly then, privity of contract can be avoided to secure a fair outcome and avoid a commercially absurd result.
>
> [27] As a general rule, the doctrine of privity provides that a contract can neither confer rights nor impose obligations on third parties. But the rule is by no means, absolute.
>
> [emphasis added]

On the basis of this reasoning, Justice Chapnik held in *PDC* that the co-defendants' claims for contribution and indemnity against the architect were limited to $250,000, stating:

> [38] B + H and Scott purchased and paid for their partial immunity as a condition of their relationship with the plaintiff. In my view, to have B + H and/or Scott now fixed with liability to make contribution in amounts exceeding the limitation for which it expressly contracted, would defeat the purpose of the limitation provision and fundamentally alter the intention of the parties and the allocation of risk negotiated by the plaintiff and B + H and Scott. It would also confer a gratuitous benefit on the co-defendants.
>
> [39] To entitle the defendants to full contribution from B + H and Scott would produce an equally absurd result as was remedied in the case of London Drugs. Certainly, if B + H and Scott were found to be the only tortfeasor liable for damages to the plaintiff, recovery would be governed by the terms of the contract.
>
> [emphasis added]

With respect to the second issue, Justice Chapnik held that by agreeing to the monetary limitation of liability, the plaintiff had waived its right to recover any amounts in excess from the other defendants. Allowing such recovery would defeat the reasonable expectations of the other parties and would unduly burden those parties.

Appeal Decision

On appeal, *PDC 3 Limited Partnership v. Bregman + Hamann Architects et al.* (2001), 52 O.R. (3d) 533, the Ontario Court of Appeal overturned the chambers decision, holding that these complex legal issues required a full hearing to consider them in complete factual context. Nonetheless, the reasoning in the initial decision is a consideration for arguing a contractual limitation to a third party claim. *PDC* resolved prior to trial without a trial decision on these issues.

Potential Acceptance of Partial Contractual Bars

Other than the somewhat analogous case of *Neale*, the reasoning in *PDC* has not been applied in other cases and it remains unclear whether a design professional, or like professional, can rely on a partial limitation of liability clause to limit a claim for contribution and indemnity to a set amount. Likewise, *Neale* has not been judicially considered, despite being an 11-year-old precedent.

Notwithstanding this lack of overt judicial consideration, in *College of New Caledonia*, Justice Parrett appears to have tacitly accepted this limitation defence thereby carving out the architect's total liability from the claim against the other defendants.

Article 3.9.1 of the AIBC client/architect agreement provided for a monetary limit to a claim, set at $250,000 per claim to the extent that such insurance is available to cover the claim. By referencing this section, in addition to the section that acted as a complete bar to the plaintiff's claim, Mr. Justice Parrett appears to have accepted that concurrent tortfeasors are limited to the contractual protections bargained for by the parties, regardless of whether those protections amount to a complete bar to a claim. However, it is important to note that this had not been judicially considered.

<u>Take Away Points</u>

After considering all of the above holdings, there are a number of take away points that are important for clients and lawyers alike. The most important considerations relate to potential agency defences and to contractual limitations, as both may result in a complete bar to a claim. Proper consideration of the scope of a party's work is required to determine whether there are potential defences.

1. Failure to advise on mitigation is attributable to the plaintiff and is a defence, not a claim against the agent.

2. Where a third party claim alleges that the party was negligent in providing due diligence warnings to the plaintiff, that claim will be considered on the same reasoning as mitigation and the fault will lie against the plaintiff;

3. Where the only negligence alleged against the third party is attributable to the plaintiff through agency, the third party claim is improper as the fault is properly apportioned to the plaintiff. In this regard, a third party claim against an agent alleging a right to contribution and indemnity under the *Negligence Act* is inappropriate because the fault lies with the plaintiff, which bars such a claim under the *Negligence Act*;

4. Where the third party claim alleges independent negligence against the agent to the claiming party, the third party claim may be appropriate;

5. If the design professional acts outside of his or her role as the plaintiff's agent, that can give rise to an independent cause of action. Counsel should focus on whether the conduct in a given case gives rise to an argument that it goes beyond the bounds of agency or outside of the scope of the agent's role;

6. If contractual limitation terms are clear and unambiguous, parties can use them to provide certainty with respect to the amount of potential liability and the time frame in which claims may be made. Courts have recognized that parties should be able to effectively manage their potential future risk and contract on a mutually agreed risk allocation basis;

7. If the potential third party has a contractual provision that is a complete bar to the plaintiff's claim, that contractual provision also creates a complete bar to claims for contribution and indemnity;

8. A limitation of liability clause that restricts a plaintiff's ability to recover to a set monetary amount or certain time period may potentially restrict claims for contribution and indemnity against the contractor to the same limited amount or time frame;

9. A subconsultant may be able to rely on limitation provisions contained in a prime contract. This may occur where the prime contract provides specific reference to the subcontractor or to the fact that a subcontractor will complete work specifically contemplated in the prime contract or where the subconsultant completes the work as an agent of the prime consultant; and

10. If a prime contract contains a monetary limitation clause, there is a potential that the entire claim against the prime contractor and the subconsultants will be limited to this set maximum amount. This defence will be highly fact specific and has received little judicial consideration.

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