GOLD SEAL Assisting Beyond Expectation

Tipsheet 14 Indemnity Clauses – Property Owners and Managing Agents

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If you are a commercial or investment property owner that outsources property management, you will be asked to sign an agreement with your managing agent.

What types of indemnities are contained in these agreements? What is the impact for your public liability insurance?

In every State and Territory, the Real Estate Institute (**REI**) has produced standard agreements for appointing a letting and property management agent (**managing agent**).

These are widely used for residential, commercial, retail and industrial properties.

Example: In NSW, the REINSW's Leasing Agency Agreement – Commercial and Industrial (FM00800) is a standard form agreement for the appointment of an agent in to manage a commercial and industrial property.

Example: In Victoria, the REIV's 'Exclusive Leasing and Managing Authority' provides 'General Conditions' for the appointment of a managing agent for residential and retail tenancies.

Example: In Qld, the REIQ's PAMD Form 20a is a standard form and terms of agreement for 'Appointment of Agent – Letting and Property Management' for the management of residential properties.

Example: In WA, the REINSW has an 'Exclusive Authority to Act as Managing Agent for Residential Premises'.

Many of these agreements contain indemnities which impact adversely on your liability insurance.

What are the duties of the managing agent?

A managing agent can be appointed to lease or rent a property on an exclusive or non-exclusive basis.

Managing agents might also agree to:

- Advertise and market the property to prospective tenants;
- Conduct background checks and select/ recommend appropriate tenants;
- Enter into, renew or cancel leases and rental/tenancy agreements on your behalf;
- Collect deposits, bonds, rent and other receipts and remit payments to you;
- Pay disbursements (eg council, sewage and water rates, insurance premiums etc.);
- Advise you of any maintenance issues relating to the property;
- Organise maintenance and repairs on an urgent basis or with your permission;
- Inspect the property prior to occupancy and ensure condition reports are completed and supplied; and
- Advise you of non-payment of rent, default by the tenant, termination of lease or vacancy of the property.

Example: A recent NSW case[i] involved a managing agent who had inspected a property owner's apartment.

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The agent did not warn the tenant or the property owner about the dangerous condition of the balcony railing.

The tenant was injured when the railing gave way 2 months after the inspection.

The court found the railing was common property and the body corporate had the primary obligation to maintain it in a good state of repair.

Usually an agent would not be liable for the inspection of a property prior to commencement of a tenancy but here the agent had agreed to conduct the inspection.

Because the agent's inspection was inadequate and it did not notify the responsible parties of the defect, the court found that the agent was 25% liable and the body corporate was 75% liable.

Does the proportionate liability legislation[ii] apply to a managing agent?

A managing agent acts as your *agent*. Both agents and property owners owe a duty of care. Traditionally, there is joint and several liability between a managing agent and you as the property owner.

The question of whether proportionate liability applies when there is an 'agency' relationship is complex because of the different proportionate liability laws.[iii]

In NSW, NT, Tasmania and Western Australia, proportionate liability would apply to a third party negligence claim if:

- An agent failed to take 'reasonable care';
- The claim is an 'apportionable'[iv] (e.g. for property damage or economic loss claim); and
- The agent and property owner have not 'contracted out' of the proportionate liability legislation.[v]

In ACT, South Australia, Queensland and Victoria, the proportionate liability legislation *may not* apply to a third party negligence claim, because the legislation does not prevent the court applying joint and several liability if there is an agency relationship.[vi]

This means the court could still find you, as the property owner, jointly and severally liable with the managing agent.

What impact does an indemnity clause have on your legal rights and liabilities?

Many Management Agency Agreements (including those prepared by the Real Estate Institutes), contain indemnity clauses that protect the managing agent.

In most cases, you have to indemnify and hold the agent 'harmless' against any legal proceedings that relate to the property management services.

Example: REINSW Leasing Agency Agreement – Commercial and Industrial (FM00800):

"The Principal will hold and keep indemnified the Agent against all actions, suits, proceedings, claims, costs and expenses whatsoever which may be taken or made against the Agent in the course of or arising out of the performance or exercise of any of the powers, duties or authorities of the Agent under this Agreement."

This type of clause transfers 100% of liability for the performance of the managing agent's duties back to you.[vii] It changes your legal liability so it is different to what it would have been under the legislation for property damage and economic loss claims. In other words, it is not consistent with proportionate liability principles.

When a clause like this appears in a contract, there is a strong argument that the parties have agreed to "contract out" of the law because the clause:

- Applies to "all actions, suits, proceedings, claims, costs and expenses" [viii];
- Doesn't reduce your liability to take account of:
    - the agent's negligence or other wrongful conduct;

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- a breach by the agent of the terms of their agency (eg a failure to comply with the agreement); or
- the extent to which the agent's other acts or omissions caused or contributed to the loss suffered by the person who has brought the legal action; and

- Prevents you from bringing a legal action against the managing agent for their failure to properly perform the services[ix].

If, for example, you have used the *REINSW contract*, proportionate liability applies to agency situations in NSW and it is permissible to 'contract out' of the proportionate liability in NSW. So this again supports the argument that you have agreed to "contract out" of proportionate liability by using that clause in your contract.

In other States and Territories[x], there are similar clauses in the REI Management Agency Agreements which can lead to similar outcomes. The exception is where the indemnity clause refers to 'proportionate liability' in some way.

Example: REIWA 'Exclusive Agency To Act as Managing Agent for Residential Premises' which states:

"The Owner hereby indemnifies the Agent against any actions, suits, demands, claims, costs, or other expenses brought against or made upon the Agent or incurred by the Agent arising out of this authority except to the extent that any relevant liability of the Agent has been caused or contributed to by the Agent's negligence or default under this agreement."

Many property owners would not be aware of this and the importance to seek legal advice on these clauses before they sign a standard REI contract.

How does an indemnity clause affect your public liability policy?

Most Management Agency Agreements require you, as the property owner, to have public liability insurance.

The insurance is designed to meet your legal liability for property damage and personal injury claims. However indemnity clauses can interfere with policy coverage if you 'assume' liability which is different to your liability at law.

This assumed liability is excluded in the 'contractual liability' exclusion that appears in most public liability policies. In other words, you are not covered for the part of an indemnity claim you "assume" under a contract.

Example: If you were a NSW property owner using the REINSW contract:

- *You have agreed to indemnify the managing agent regardless of their fault; and*
- *The proportionate liability legislation applies in the absence of the indemnity clause.*

If for example, the managing agent is negligent in performing its duties and liable to compensate someone for property damage, you may be obliged to pay the compensation because of the indemnity clause.

Your insurer can refuse to pay your claim for compensation if you don't have any liability at law - you assumed the liability under a contract. In other words, the 'contractual liability exclusion' in the policy allows the insurer to deny the claim. It also applies where you have liability for part of the claim but the managing agent has liability for the rest.

This means you may have an 'uninsured loss' for the managing agent's share of the claim.

There could be a similar problem for NT, WA and Tasmanian property owners (depending on the terms of their Management Agency Agreement).[xi]

For ACT, Qld, SA and Victorian property owners, the impact may be less significant because they can still be jointly and severally liable for the negligence of the managing agent due to the operation of agency law. However there is a risk for them if the court rules that proportionate liability applies.

Managing agents are required by law to hold professional indemnity insurance. However the indemnity clauses in many REI Management Agency Agreements mean the property owner

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cannot bring a professional negligence claim against the managing agent![xii]

How do you protect against this?

- Don't sign a Management Agency Agreement that contains an indemnity clause without getting advice. It may trigger the 'contractual liability' exclusion in your public liability policy.
- Before you sign a Management Agency Agreement, send it to your broker. Your broker can access lawyers who can advise on the issues raised in this Tipsheet.
- Speak to the managing agent about this issue because you may need to change the indemnity clause to ensure your insurance policies are not adversely affected.
- If you have already signed an REI Management Agency Agreement, contact your broker immediately. If the clause is a problem and it can't be changed, there may be other things your broker can do to minimize the risk of an insured claim.

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[i] *Wu v. Carter* [2009] NSWSC 355

[ii] See our Tipsheet 3 on proportionate liability. Ask your broker for a copy.

[iii] For this reason, the Standing Committee of Attorney Generals has undertaken a review of the proportionate liability legislation with a view to introducing a uniform Model Law which will be adopted in every state and territory. They commissioned a report from Emeritus Professor J L R Davis ('Proportionate Liability: Proposals To Achieve National Uniformity') which recommends that proportionate liability legislation should not apply to agency.

[iv] See Tipsheet 3 on proportionate liability for details on what is an 'apportionable claim'. Ask your broker for a copy.

[v] Remember in some states and territories it is possible to 'contract out' of the legislation (NSW, Tasmania and WA). In other states the legislation is silent on this point so it is unclear whether 'contracting out' is permitted (SA, ACT, NT and Victoria). Only in Qld is it unlawful to contract out of the legislation. See Tipsheet 3 on proportionate liability.

[vi] In those states and territory, there is a provision in the law that states that proportionate liability legislation does not prevent a person from being held jointly and severally liable for damages awarded against another person as agent of the person. This means the court can still make a finding of joint and several liability was between an agent and its principal.

[vii] A recent New South Wales case, *Laresu Pty Ltd v Clark* (NSWCA, 4 August 2010) considered the REINSW contract in this Tipsheet. On that occasion, the Court of Appeal ruled that the indemnity clause was not operative because it only indemnified the agent for performance of its duties - not a failure to perform those duties. In that case, the agent was held 60% liable for a personal injury compensation claim due to a breach of the agent's duty of care regarding its failure to inform the property owner of the safety risks relating to the owner's decision to automatically switch off lighting in the premises at 6.30pm every evening.

[viii] Applying the rationale in the Tasmanian case of *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3, if the property owner has agreed to keep indemnified the managing agent from "all actions, suits, proceedings ,claims etc..", there is an argument that the parties did not want proportionate liability legislation to apply.

[ix] This is because if the property owner was to make a claim along those lines, the managing agent could invoke the indemnity clause to require the principal to indemnify them for the claim.

[x] For example in Qld, the indemnity clause in PAMD Form 20a is much more detailed but it still has a 'catchall' clause stating: "*The Client indemnifies the Agent from and against all actions, claims, demands, losses, costs, damages and expenses arising out of or in respect of this Agreement from…the Agent acting on behalf the Client under this Agreement."*

[xi] If they have used the example REIWA contract which recognises proportionate liability – this won't be a problem.

[xii] This is because the property owner is holding the agent harmless in the indemnity clause in the contract.

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