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Contractual Indemnification Clauses - Part II
"The Ramifications"

This is the second of two parts in our Newsletter dealing with the topic of Contractual ("Express") Indemnification Clauses. In the first part we discussed the general virtue of such clauses as well as the three broadly classified types and their implications.

Problems with indemnity agreements normally arise when one party seeks to shift a disproportionate or unfair amount of risk on a given project or in a given undertaking that would be disproportionate to the other party's ability to control the risk or to otherwise agree to be responsible for it. It is not uncommon, for example, for an owner to receive counsel to attempt to contractually shift risk to contractors and/or designers believing that it will relieve itself of a certain amount of claim or lawsuit activity on its projects. If such attempted transfer of risk is grossly unfair or arbitrarily imposed, because of a disparate bargaining power in the contract negotiations, an owner may simply incur additional expenses and effort to attempting to enforce the unfair agreement while still having to deal with the consequences of the third party claim that gave rise to it.

Legal counsel for contractors and designers will frequently recommend against agreeing to specific indemnity clauses. In addition, contractor insurers may provide contractual coverage for indemnity clauses and may also agree to add indemnitees as additional insureds. Professional liability insurers generally will do neither and will usually specifically exclude coverage for indemnity agreements (please see below). As mentioned above, rights of comparative or implied indemnity are generally recognized to exist independent of any specific contractual undertaking and are philosophically based upon the idea of fairness. If it is absolutely necessary to agree to contractually indemnify another party, however, a Type Three clause is generally preferred although a Type Two clause may also be acceptable. It is important, in any event, not to sign any agreement without a thorough understanding of its terms and without reviewing the clause with an insurance carrier whose policy coverage may be affected by it. It goes without saying that it is always wise to contact legal counsel to discuss the true impact of such a proposed indemnity clause and also to seek additional compensation from the proposed indemnitee for the undertaking itself.

As referenced above, professional liability insurers generally specifically exclude coverage for contractual indemnification clauses in their policy holders' contents for many of the same reasons that preclude clients becoming "Additional Insureds" under this type of insurance coverage (please see prior newsletter Volume 17, Issue 4). In addition, as a practical matter, the obligation to provide a defense that is normally a part of such undertaking is problematic for an insurer. Among other reasons, this is because the usually convoluted and complex nature of construction litigation is such that the liability of the parties are seldom clear and may frequently be in conflict, so the design professional's insurer should not be

compelled to defend the interests of a party whose interests are almost certainly adverse to those of its policyholder, while contributing to the exhaustion of its deductible and insuring limits.

Finally, express indemnity clauses are provided in many standard contract forms such as the American Institute of Architects General Conditions of the Contract for Construction, A201 (1997), under Clause 3.18.1. Additionally, state laws or codes such as California Civil Code Section 2772, et seq., provides rules for the interpretation and application of express contractual indemnity clauses.

Coming Next Quarter: The "Spearin Gap"

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