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Bulletin #87, Indemnification Agreements – "You Want Me to Pay for What?" (May 24, 2005)

A subcontractor naturally expects to undertake certain risks when signing a subcontract. A subcontractor's risks include the possibility of incurring damages for delay, repair costs, or personal injury and property damage resulting from the subcontractor's own negligence or the negligence of one of its employees. Subcontractors, generally, do ***not*** expect to be liable for damages caused by the conduct of the general contractor, owner, or another subcontractor. However, a subcontractor can be liable when signing a broad indemnification agreement without first determining the consequences of such an agreement.

Indemnification:
A Promise to Insure Against the Loss and/or Damage Suffered by Another

Ideally, a subcontractor should seek to avoid agreeing to indemnify a general contractor, and should include contractual language specifically excluding any obligation to indemnify. Practically, the vast majority of subcontracts include an indemnification provision and most subcontractors do not have sufficient bargaining power to exclude such a provision. Nevertheless, it is important to understand the consequences of an indemnification provision before signing the agreement. Furthermore, as the laws vary from state to state, it is important to seek legal counsel to review the specific laws for the state governing your agreement.

(It is important to keep in mind that this Contracts Bulletin is only a general overview of the law in this area. Because laws in individual states vary and the facts that circumstances of each case will determine the nature and extent of a subcontractor's liability, it is recommended that you seek competent legal advice before signing an agreement to indemnify.)

What is an Indemnification Agreement?

An indemnification agreement provides that the subcontractor will pay for the general contractor's losses if the general contractor is liable to a third party. For example, a general contractor may be sued by a worker injured on a job site and forced to pay damages to the injured worker. The subcontractor may be responsible to reimburse (or indemnify) the general contractor for all of the money the general contractor paid to the worker. (An indemnification agreement may also be referred to as a "hold harmless" agreement.) When a general contractor seeks "contribution" from a subcontractor, it is asking the subcontractor to pay for a portion of the money the general contractor owes to the injured worker.

A duty to indemnify usually arises as the result of a contract between two parties. In all likelihood, the majority of subcontractors sign contracts that contain standard indemnification clauses. A duty to indemnify can also be implied by the nature of the relationship between two parties. In those situations, the claim is

often called “equitable indemnification” because it arises out of an obligation to do what is equitable or fair. The scope of the responsibility of the subcontractor is determined by the language of the indemnification agreement and the laws of the particular state.

What Damages Do I Have to Pay For?

So when does a subcontractor have to provide indemnification? Well, it depends on the state.

If the indemnification agreement is governed by New York laws, the subcontractor will have a more limited duty to indemnify. New York has some of the most restrictive laws in the United States governing indemnification agreements. In other states, more deference is given to the parties’ agreement and the question hinges on the language in the indemnification agreement itself. Because the laws vary so greatly from state to state, it is impossible to provide a general statement regarding how particular indemnification agreements will be viewed by the courts. Consequently, what follows is an overview of cases in various states dealing with indemnification agreements. The results in these cases underscore the need to understand the language of an indemnification agreement and the laws applicable to the agreement before signing it.

Indemnification for a Party’s Own Negligence

Under the laws of most states, a subcontractor will not be forced to indemnify a general contractor (or owner) against damages caused by the general contractor’s (or owner’s) own negligence unless the parties’ agreement clearly and explicitly provides for such indemnification. Examples of one–sided indemnification clauses that place substantial responsibilities on subcontractors, even for the negligence of the general contractor, include:

> Subcontractor shall indemnify General Contractor regardless of whether the claimant has filed suit on the claim. Subcontractor’s duty to indemnify General Contractor shall arise even if the General Contractor is the only party sued by the claimant and/or claimant alleges the General Contractor’s negligence was the sole cause of the claimant’s damages.

As is evident with the above clause (which was pulled from an actual home construction subcontract agreement), substantial liabilities may be placed on subcontractors through indemnification clauses, even when the responsibility for fault lies with the general contractor.

In those states, such agreements run afoul of public policy and are generally found to be either entirely or partially unenforceable. These states place a high priority on parties taking responsibility for damages caused by their own actions. In addition, forcing a party to be responsible for damages caused by its negligence encourages the party to take accident prevention measures, which are important in an industry that carries an inherent danger of such accidents occurring.

New York

In 1997, New York considered two cases in which the indemnification agreements required the subcontractors to indemnify the general contractors for all losses, even those caused by the general contractor’s negligence. Itri Brick & Concrete Corp. v. Aetna Casualty & Surety Co., 680 N.E.2d 1200 (N.Y. Ct. App. 1997). Itri was a masonry subcontractor on a project. One of Itri’s employees was injured on the job and sued the general contractor. The general contractor sued Itri for indemnification. The parties agreed that the general contractor was 24.25% negligent and that Itri was 75.24% negligent. The indemnification agreement in Itri’s contract required Itri to indemnify the general contractor against all liability for claims of injury or death that arose from activity at or near the project, notwithstanding any responsibility of the general contractor.

Similarly, Shopovick was a carpentry subcontractor working on a construction project. One of Shopovick’s employees was injured and sued the general contractor, who, in turn, sued Shopovick for

indemnification. The jury found that Shopovick was 50% negligent, the general contractor was 35% negligent, and the employee was 15% negligent. The indemnification agreement in the contract required Shopovick to indemnify the general contractor for all claims that arose from the work without regard to whom or what caused the injury.

The court found that, under New York law, both of the indemnification agreements were void. The agreements attempted to broaden the liability of the subcontractors by imposing liability, without limitation, for the negligence of the general contractor or owner. The language in the agreements was contrary to New York law, which prohibits agreements to indemnify for another's negligence. The purpose of the law was to prevent the prevalent practice of requiring the subcontractors to assume liability for the negligence of others. The parties argued that the agreements should be partially enforced to the extent that the damages were not caused by the general contractor's negligence. However, because the agreements did not include language limiting the subcontractor's liability to that permitted by law, or to the subcontractor's negligence, the agreements were found to be entirely unenforceable.

Missouri

Other states will partially enforce indemnification agreements to the extent that the damages were not caused by the general contractor's negligence.

In 2003, the Missouri Supreme Court considered a broad indemnification provision in a subcontract. Nusbaum v. City of Kansas City, 100 S.W.3d 101 (Mo. 2003). A theater patron fell on one of the theater's walkways and was injured. The patron brought suit against a number of entities, including the general contractor (Dunn) of a neighboring construction project and its subcontractor (PC). Dunn sought indemnification from PC, relying on an indemnification agreement in the parties' contract. PC argued that it should not be held responsible because the indemnification agreement did not require it to indemnify Dunn against Dunn's negligence. Dunn disagreed and argued that the indemnification agreement was intended to indemnify Dunn against all claims regardless of the cause. The Missouri Supreme Court agreed with PC. The court ruled that it would not construe an indemnification agreement to provide indemnification for a party's own negligence unless the parties have clearly expressed an intention to do so. Consequently, PC was only responsible for the damages that did not result from Dunn's negligence.

Indemnification Where Neither Party is Negligent

Depending on the language of the indemnification agreement, a subcontractor may be required to indemnify a general contractor in situations where neither the general contractor nor the subcontractor is negligent.

The California Court of Appeals considered such a situation in 2000. Centex Golden Construction v. Dale Tile Co., 93 Cal.Rptr.2d 259 (Ca. Ct. App. 2000). Centex was the general contractor responsible for the construction of a commercial building. Dale was the tile subcontractor on the project. Following completion of the project, the owner brought a number of claims against Centex. One of the claims was for defective tile work. Centex brought an action against Dale for reimbursement of the money it paid to the owner on the owner's tile claim. The indemnification agreement between Centex and Dale required Dale to indemnify Centex for any claims, liability, losses, damages, costs, and expenses unless they resulted from the sole negligence or willful misconduct of Centex.

As part of the trial on Centex's indemnification claim, the jury considered whether Centex or Dale was negligent. The jury found that neither was negligent. Dale argued that it could not be required to indemnify Centex unless Centex could demonstrate that Dale was negligent. The court agreed with Centex and noted that the indemnification agreement only excluded claims that resulted solely from Centex's negligence or misconduct. In this situation, the jury found that Centex was not negligent. Consequently, Dale was required to indemnify Centex.

Agreement to Provide Insurance

Even though a subcontractor may not be required to indemnify a general contractor against the general contractor's negligence in some states, the subcontractor may still be required to provide insurance to cover the general contractor's negligence pursuant to the parties' contract. Watson–Forsberg Co. v. Pro–Tech Roof Sys., Inc., 488 N.W.2d 473 (Minn. 1992).

Watson–Forsberg was the general contractor on a construction project. Pro–Tech was the roofing subcontractor. One of Pro–Tech's employees was injured when he slid down the roof and fell to the ground. The employee sued Watson–Forsberg, alleging that it was negligent in failing to inspect the premises for unsafe conditions, failing to warn the employee of the unsafe condition, and failing to remove snow and ice from the roof prior to directing Pro–Tech to begin its work. Watson–Forsberg, in turn, sued Pro–Tech for indemnification under the parties' subcontract.

The contract required Pro–Tech to indemnify Watson–Forsberg for all damages and injuries to the fullest extent allowed by law. The agreement further required Pro–Tech to obtain insurance coverage to insure against the claims contemplated in the indemnification provision. Pro–Tech argued that the agreement was unenforceable because Minnesota only allows a party to indemnify another against the party's own negligent or wrongful acts. However, the court ruled that Pro–Tech's argument ignored the "long–standing practice in the construction industry by which the party would purchase insurance that would protect 'others' involved in the performance of the construction project." The court distinguished an agreement to provide insurance from an agreement to indemnify. The court found that an agreement to provide insurance is enforceable.

Practical Considerations

It is important to carefully review indemnification provisions and, if possible, limit their scope before signing a subcontract. Although some states disallow indemnification clauses that are not limited to coverage for damage caused by the negligence of the subcontractor, many states only bar broad indemnification clauses. In those states, the subcontractor will have to provide indemnification unless the general contractor is solely responsible. Furthermore, some states will enforce an agreement requiring a subcontractor to indemnify a contractor against the contractor's own negligence if the language is clear and unequivocal. Finally, some states will enforce an agreement to obtain insurance for a general contractor's negligence even if an indemnification agreement covering the same type of loss would be unenforceable. The key is understanding the scope of the indemnification agreement before you sign it.

Conclusion

In an ideal situation, subcontractors would avoid signing indemnification agreements entirely. Unknowingly signing a broad indemnification agreement could result in staggering risks. However, at minimum, it is important to take steps (including contacting your lawyer) to understand the implications of the particular indemnification agreement, in light of the law in the state governing the agreement, and minimize the resulting risks whenever possible.

SMACNA wants the Contracts Bulletins to serve our members. Your feedback or topic suggestions are welcomed by contacting Steve Yoch (e–mail: syoch@felhaber.com; telephone 651 312 6040) or Tom Soles, SMACNA's Executive Director – Market Sectors, (e–mail: tsoles@smacna.org; telephone: 703 803 2988).

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