

Contractual Indemnification in Construction

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Summary

- What is an indemnification clause:
 - RISK ALLOCATION – Obligates one party (the Indemnitor) to reimburse a second party (the Indemnatee) for the losses that Indemnatee incurs, or the damage for which it may be held liable
 - Indemnification clauses are used to transfer liability for property loss and bodily injury , damages and/or judgments, transfer the duty to defend, and transfer or allocate the duty to insure.
 - Shifts the risk from upstream parties (Owners, architect, engineers) to subcontractors
- There are Two Types of Enforceable Indemnification Provisions in Arizona Private Work Construction Contracts
 - General – everyone responsible for their own mistakes (Proportional Liability)
 - Specific – Subcontractor must pay for everything even if the contractor is 99.9% at fault (gross generalization)

Summary

- **How Do I Know What I am Signing?**
 - In Arizona there are a few key phrases lawyers use for Specific Indemnification. Know the key phrases
- **Where Do Lawyers Hide This Language?**
 - In addition to the Indemnification and Insurance Sections; additional language can be hidden in Exhibits and Safety Provisions.
- **Is Negotiation Possible?**
- **Can't We Change the Law?**

Why Is This Important?

- Do you want to make a profit?
- Do you want to pay for the Upstream Contractor's attorneys' fees?
- Do you want to pay for Upstream Contractor's mistakes?
- Insurance does not cover all risks.
- What if one of the other subs on the job goes out of business?

OSHA Investigation (Example)

- Your employee is injured at the workplace (scissor lift fell into hole.) General Contractor was actively negligent - accident was not entirely your fault.
- ADOSH investigator cites Sub and the GC but the GC wants to fight the charge.
- If you entered into a subcontract agreement with a specific indemnity provision – you might be left paying \$500 plus an hour on a lawyer and for the fine levied against the contractor.
- CGL Policy is not going to cover these costs.



Amberwood Development v. Swann's Grading, Inc.

- Construction Defect – Residential Subdivision
- Subcontract Indemnification Provision:
 - Subcontractor agrees to and does hereby hold Contractor harmless from any and all claims, actions, damages, costs or Attorney's fees arising out of the acts or omissions of Subcontractor, its employees, agents or suppliers with regard to the performance or omission of any of Subcontractor's duties and obligations under this contract. The indemnity extends to any claims asserted by any subsequent property owner alleging improper or defective workmanship or materials in any work or material done or provided by Subcontractor.
- Swann's subcontract required it to indemnify Amberwood for any claims arising out of or connected to Swann's work, not merely those caused by Swann's negligent acts or omissions.

2 Types of Valid Contractual Indemnification in Arizona (Currently)

Specific Indemnification

- Bad for Subs
- Good for Owners and General Contractors

General Indemnification

- Okay for Subs

General Indemnification

- Also known as a limited indemnification or proportional indemnification
- You are responsible for your screw up. If another party pays for your mistake; you need to indemnify (pay them) for the percentage of your fault.
- Example: “The subcontractor shall indemnify Contractor from any claims to the extent caused by subcontractor’s performance of this contract.”

Arizonans for Fair Contracting



Your Voice for Fair Contracting in Arizona

www.azfaircontracting.com

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SB 1338

- 2017 Legislative Session
- Arizonans for Fair Contracting working with Arizona State Senator Karen Fann (Prescott) crafted legislation
- This specific bill will not advance. It serves as the vehicle to begin the process and to galvanize supporters.
- Sec. 3 Legislative Intent (B): It is the intent of the legislature to extend the provisions governing proportional liability in public contracting. This will ensure fairness in construction contracting between general contractors and subcontractors and will create an economic climate that will promote safety in construction, foster the availability and affordability of insurance and reduce the legal costs associated with construction claims.

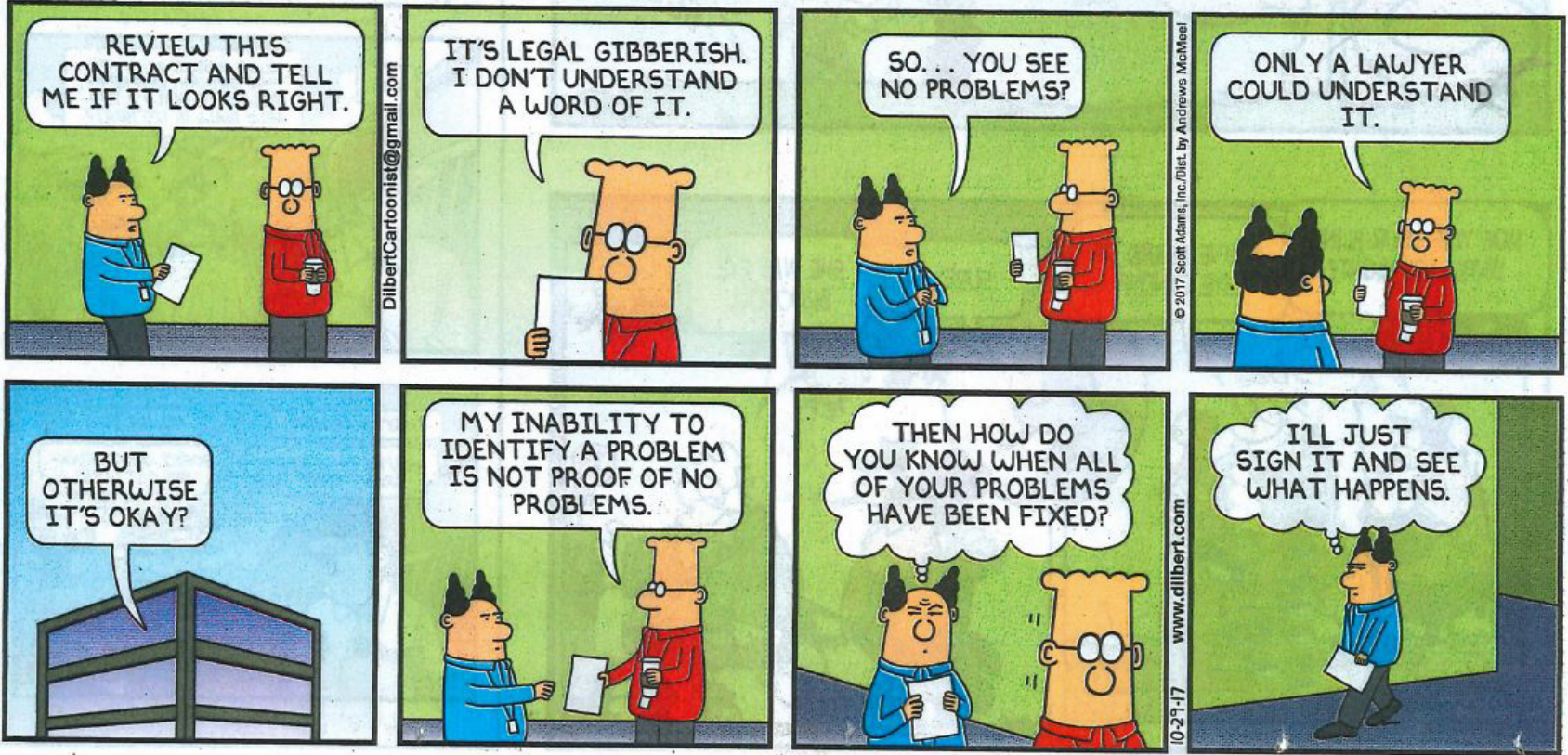
ARS 34-226 (public works)

- A subcontract or design professional services subcontract entered into in connection with a public building or improvement may also require any subcontractor or design professional to indemnify and hold harmless the agent and that contractor, subcontractor, or design professional who executed the subcontract, and their respective owners, officers and employees, from liabilities, damages, losses and costs, including reasonable attorney fees and court costs, but only to the extent caused by negligence, recklessness or intentional wrongful conduct of the indemnifying subcontractor or design professional, or other persons employed or used by the indemnifying subcontractor or design professional in connection with the subcontract.

Ariz. Rev. Stat. Ann. § 34-226

What are we trying
to avoid?

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Specific Indemnification

- Provides indemnification for the Up Stream Participant's active negligence
- Where a specific indemnification agreement applies, indemnification obligations will be provided even where the party is 99.9% responsible.
- Your negligence might be irrelevant (Swann's Grading)
- Any construction contract provision that indemnifies, holds harmless the promisee from or against liability for damage resulting from the promisee's sole negligence is void. ARS 32-1159.

Example

ARTICLE 10. INDEMNITY

Subcontractor shall defend, indemnify and hold Contractor and Owner and their agents and employees harmless from all claims, injuries, damages, liability, losses, costs, penalties, expenses and fees (including without limitation attorneys' fees) in any way arising out of or resulting from Subcontractor's performance of the Work pursuant hereto, including without limitation any claims, liabilities, losses, costs, expenses and fees associated with the furnishing of labor, materials or rental equipment to or for the benefit of Subcontractor and from any violation or fees associated with the furnishing of labor, materials or rental equipment to or for the benefit of Subcontractor and from any violation or fees associated with the furnishing of labor, materials or rental equipment to or for the benefit of Subcontractor and from any violation or infringement or claimed violation or infringement of patent, trademark or other similar rights:

(a) caused in whole or in part, or alleged to have been caused in whole or in part, by any negligent act or omission of Subcontractor or any of its agents, employees or subcontractors or anyone directly or indirectly employed by them, or

(b) caused by any act or omission of Contractor or Owner, or their agents and employees, whether actively or passively, which may have in part contributed to any such claims, injuries, losses, damages, except for the sole negligence of Contractor and/or Owner.

This indemnity shall include any damage to Contractor's property, or by reason of any injury to or death of Contractor's employees, Subcontractor's employees or to third persons or damage to their property. THIS AGREEMENT OF INDEMNITY EXPRESSLY INDEMNIFIES CONTRACTOR AND OWNER AGAINST ALL LIABILITY, CLAIMS, SUITS, DAMAGE, LOSS, JUDGMENT OR EXPENSE, INCLUDING ATTORNEY'S FEES, WHICH CONTRACTOR OR OWNER MIGHT INCUR BECAUSE OF CONTRACTOR'S OR OWNER'S NEGLIGENT FAILURE TO DISCOVER OR REMEDY A DANGEROUS CONDITION CREATED BY SUBCONTRACTOR.

In no event shall Subcontractor be required to indemnify Contractor and/or Owner in excess of that permitted under the public policy of the situs of the Project. Subcontractor shall reimburse Contractor and/or Owner, their agents and employees any and all legal expenses incurred by each of them in enforcing any of the indemnities provided for in this Subcontract.

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(a) Caused
in whole or
in part

...Whether actively or...
...Except for the sole negligence...

(b) caused in whole or in part by the negligent act or omission of Contractor or Owner, or their agents and employees or subcontractors or anyone directly or indirectly employed by any of them, or anyone for whose conduct they may be liable, whether or not such claim, injury, loss, damage, expense or cost was caused in part by the active or passive negligence of Contractor and/or Owner.

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Another Example

Subcontractor (or its sub-subcontractor(s) as the case may be) acknowledges and agrees that it has the primary responsibility for the safety as

well as the safe operations of its own employees and the employees of its sub-subcontractors, its agents and its business and non-business invitees (hereinafter collectively referred to as "such persons"). Included in this responsibility is the obligation to provide safe working conditions for all such persons.

Accordingly, the Subcontractor (or its sub-subcontractor(s) as the case may be) agrees to indemnify and hold harmless the Contractor, Owner and Architect/Engineer and their officers, employees and agents of each against any and all claims, damages, losses, expenses, liability or cost (including reasonable attorney's fees, court costs and any other costs of litigation) (hereafter collectively referred to as "losses") for bodily injury, including death and property damage, including loss of use, arising in any manner out of the performance of the Work included in this Subcontract. However, to the extent that such losses to the Contractor or Owner or officers, employees, and agents of each are caused by the direct, active sole negligence of any employee or agent of the party seeking indemnification, the Subcontractor shall not be responsible for any such losses.

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Another Example

- INDEMNITY: Subcontractor agrees to and does hereby hold Contractor harmless from any and all claims, actions, damages, costs or Attorney's fees arising out of the acts or omissions of Subcontractor, its employees, agents or suppliers with regard to the performance or omission of any of Subcontractor's duties and obligations under this contract. The indemnity extends to any claims asserted by any subsequent property owner alleging improper or defective workmanship or materials in any work or material done or provided by Subcontractor.
- To the fullest extent permitted by law, Subcontractor shall defend and indemnify and hold harmless, Contractor and their agents and employees from claims, demands, costs, attorney fees, causes of action and liabilities of every kind whatsoever arising out of or in connection with Subcontractor's work performed for Contractor. This defense and indemnity shall extend to claims occurring after this agreement is terminated as well as while it is in force. The defense and indemnity shall apply regardless of any active and/or passive negligent act or omission of the Contractor, Architect, or their agents or employees, but Subcontractor shall not be obligated to indemnify any party for claims arising from the sole negligence or willful misconduct of the Contractor or its agent or employees. The defense and indemnity set forth in this section shall not be limited by any insurance requirements, or by any provision of this Agreement. All work done at a site or in preparing or delivering materials or equipment to the site shall be at the sole risk of Subcontractor until the work is accepted by Contractor.

Includes a Duty to Defend

32. To the fullest extent permitted by law, Subcontractor shall indemnify, defend (at Subcontractor's sole cost and expense and with legal counsel approved by Contractor and/or Owner, which approval shall not be unreasonably withheld), protect and hold harmless Contractor and/or Owner, all subsidiaries, divisions and affiliated companies of Contractor and/or Owner, and all of such parties' representatives, partners, designees, officers, directors, shareholders, employees, consultants, agents, successors and assigns, and any lender of Owner with an interest in the Project (collectively, the "Indemnified Parties"), from and against any and all claims (including, without limitation, claims for bodily injury, death or damage to property), demands, obligations, damages, actions, causes of action, suits, losses, judgments, fines, penalties, liabilities, cost and expenses (including, without limitation, attorneys' fees, disbursement and court costs, and all other professional, expert or consultants' fees and costs and Contractor's and/or Owner's general and administrative expenses) of every kind and nature whatsoever (individually, a "claim"; collectively, "claims"), which may arise from or in any manner relate (directly or indirectly) to any work performed or services provided under this Subcontract Agreement (including, without limitation, defects in workmanship or materials and/or design defects [if the design originated with Subcontractor]) or Subcontractor's presence or activities conducted on the Project (including, without limitations, the negligent and/or willful acts, errors and/or omissions of Subcontractor, its principals, officers, agents, employees, vendors suppliers, consultants, sub-consultants, subcontractors, anyone employed directly or indirectly by any of them or for whose acts they may be liable or any or all of them) regardless of any active or passive negligence or strict liability of an Indemnified Party. Subcontractor understands and acknowledges that the indemnification obligation hereunder is intended to constitute "specific" indemnity under Arizona law and extends to and includes claims arising from the active or passive negligence of Indemnified Parties. Notwithstanding the foregoing, nothing herein shall be construed to require Subcontractor to indemnify the Indemnified Parties from any Claim arising from the sole negligence or willful misconduct of the Indemnified Parties.

33. The duty to defend hereunder is wholly independent of any separate from the duty to indemnify and such duty to defend exists regardless of any ultimate liability of Subcontractor. Such defense obligation shall arise immediately upon presentation of a Claim by any party and written notice of such Claim being provided to Subcontractor. Payment to Subcontractor by any Indemnified party or the payment or advance of defense costs by any Indemnified Party shall not be a condition precedent to enforcing such Indemnified Party's rights to indemnification hereunder. Subcontractor's indemnification obligation hereunder shall survive the expiration or earlier termination of this Subcontract Agreement until such time as action against the Indemnified Parties for such matter indemnified hereunder is fully and finally barred by the applicable statute of limitations. Subcontractor's liability for indemnification hereunder is in addition to any liability Subcontractor may have to Contractor and/or Owner for a breach by Subcontractor of any of the provisions of this Subcontract Agreement. Under no circumstance shall the insurance requirements and limits set forth in this Subcontract Agreement be construed to limit Subcontractor's indemnification obligation or other liability hereunder. The terms of this Subcontract Agreement are contractual and the result of negotiation between the parties hereto. Accordingly, any rule of construction of contracts that ambiguities are to be construed against the drafting party shall not be employed in the interpretation of this Subcontract Agreement.

Look out for this Trick

ARTICLE 9 - GENERAL INDEMNITY

9.1 To the fullest extent permitted by law, Subcontractor, at its sole expense, shall defend, indemnify and hold Contractor, Owner, and Contractor's and Owner's officers, directors, agents, employees, successors and assigns (hereinafter "Indemnified Parties") harmless from any and all claims, injuries, damages, liability, losses, costs, penalties, expenses and fees (including without limitation attorney' fees, court costs and expert witness fees) in any way arising out of or resulting from Subcontractor's performance of the Work including, without limitation, any claims, liabilities, losses, costs, expenses and fees associated with the furnishing of labor, materials or rental equipment to or for the benefit of Subcontractor (i) caused in whole or in part by any negligent or intentional act or omission of Subcontractor, or any of its agents, employees or subcontractors or anyone directly or indirectly employed by them; or (ii) caused by any act or omission of Indemnified Parties, whether actively or passively, which may have in part contributed to any such claims, injuries, losses, damages, except for the sole negligence or willful misconduct of Contractor and/or Owner (the "Indemnity").

And Another

SECTION 23- GENERAL INDEMNIFICATION

A. The Subcontractor shall protect, indemnify, hold harmless, and defend the Contractor, the Owner, the Architect/Engineer, the Construction Manager, and any of their respective employees and agents (the “Indemnitees”) against any and all claims, causes of action, suits, losses, costs, or damages, including attorneys’ fees, resulting from the acts, failure to act, omissions, negligence, or fault of the Subcontractor, those employed by it, or its agents, whether or not said claim, cause of action, suit, loss, cost, or damage is alleged to be caused in part by any act, failure to act, omission, negligence, or fault of any of the Indemnitees or their employees, and Subcontractor shall bear any expense which any of the Indemnitees may have by reason thereof, or on account of being charged with such claim, cause of action, suit, loss, cost or damage, unless such claim, cause of action, suit, loss, cost, or damage is solely caused by the Indemnitee’s sole act, failure to act, omission, negligence, or fault.

Be On the Lookout For

- “Active Negligence”
- “Caused in whole or in part”
- “To the fullest extent permitted by law”
- “Except for Sole Negligence”
- “Arising Out Of”



Where Should You Be Looking?

- Indemnification Provision
- Safety Section – Possibly in an exhibit
- Insurance Provision
- General Conditions
- Prime Contract



Other Issues

- **Duty to Defend**
 - You do not want to agree to defend a general contractor or owner using counsel approved by the owner or general contractor in its sole discretion
 - Could be contrary to your insurance policy

So What Language Is Better?

Accordingly, the Subcontractor agrees to indemnify and hold harmless the Contractor, Owner and Architect/Engineer and their officers, employees and agents of each against any and all claims, damages, losses, expenses, liability or cost (including reasonable attorney's fees, court costs and any other costs of litigation) (hereafter collectively referred to as "losses") for bodily injury, including death and property damage, including loss of use, arising in any manner out of the **NEGLIGENT** performance of the Work included in this Subcontract. **However, to the extent that such losses to the Contractor or Owner or officers, employees, and agents of each are caused by the negligence of any subcontractor, employee or agent of the party seeking indemnification, the Subcontractor shall not be responsible for any such losses**

What Language Is Better?

Limit the Indemnification: “To the extent caused by the negligent act of the subcontractor”

To the extent caused by is more limited than “arising out of”

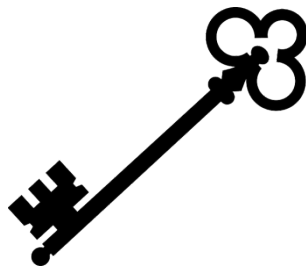
Contractor shall indemnify Owner from and against any losses incurred by Owner, but only to the extent such loss was incurred as a result of Contractor’s misconduct or negligent acts or omissions with respect to the Work and not due in whole or in part to the breach, negligence or misconduct of Owner.

Can You Actually Negotiate These Terms?

- Absolutely
 - Trades currently hold the cards
 - Lots of work and not enough labor to go around
 - Fighting back on these provisions could help the effort to change the law
- States like California do not allow specific indemnification. California Civil Code 2782(c). This is not unheard of.
- Less likely when dealing with large national general contractors but does not mean you should not try
- Agree to meet in the middle - limit your indemnification to the limits of CGL Insurance. – Don't agree to indemnify for claims arising out of your work.

Consistency is Key

- Look out for the Exhibits.
- Make sure you have not missed a safety provision.
- Everything needs to be consistent.



In Case You Cannot Modify the Provision

- Make sure your downstream subs are providing you with specific indemnification
- Check with your broker to make sure there are no exclusions in the policy that you need to know about.
- Make sure your subs are licensed, bonded, insured. And get a list of all the other subs on the job so if the sh*t hits the fan – you know from whom to seek equitable contribution.

SacksTierney P.A.

ATTORNEYS

Questions?

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Thank you!



Brian M. Flaherty

Brian focuses his practice on construction and insurance coverage matters and commonly represents subcontractors in disputes with general contractors, private owners and the government. He has successfully represented contractors in disputes over prompt payment, change orders, delay damages and termination. He also represents contractors and construction professionals in licensing matters and administrative hearings involving the Arizona Registrar of Contractors and other government agencies.

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