Indemnification Contracts - Some Suggested Problems and Possible Solutions

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INDEMNIFICATION CONTRACTS—
SOME SUGGESTED PROBLEMS
AND POSSIBLE SOLUTIONS

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Indemnification agreements in construction or remodeling contracts, leases and the like, take various forms. All are generally directed toward securing indemnification from a contractor or lessee against liability to the property owner for damage to property or injuries arising out of the contractor’s repairs or construction on or about the owner’s premises, or arising out of the lessee’s operations.

The question arises whether the indemnification agreements protect the owner in cases where negligence of its own employees may have caused or contributed to the accident and the resulting damages. An indemnification agreement is to be distinguished from an exculpatory clause. “An exculpatory clause is one which excuses one party from liability for otherwise valid claims which may be made against him by another. Third parties are not involved.”

“An Indemnification or Hold Harmless Agreement... is an agreement whereby one party to a lease or other contract agrees to protect the other from claims for loss or damage made against the indemnitee by a third party.”

The law varies from state to state with regard to the enforceability of indemnification contracts. Generally they are enforceable even where the negligence of the party securing the indemnification (the indemnitee) causes or contributes to causing the damages. However, indemnification agreements are interpreted to extend to such cases only if the contract expressly states that it applies where the indemnitee is negligent. The courts generally have been very hesitant to interpret in-

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1 Lewy, The Use of Exculpatory Clauses Affecting Real Property, Leases, and Hold Harmless Agreements and the Insurance Implications Involved, 46 Chi. B. Record 131 (Dec. 1964).

2 Ibid.

3 See Annot., 143 A.L.R. 312, 316 (1943) and Annot., 175 A.L.R. 8, 30 (1943); 27 Am. JUR. Indemnity §15 (1940). It is noted that 27 Am. JUR. Indemnity, §9 (1940) stated the majority of courts held such indemnification agreements void, but in the 1965 Pocket Part Supplement to the section, the opposite rule is stated as follows: “A contrary view is taken by the great majority of modern cases.” See Restatement, Contracts §§572 (1932), and Thompson-Starrett Co., Inc. v. Otis Elevator Co., 271 N.Y. 36, 2 N.E. 2d 35 (1936). In Hollingsworth v. Chrysler Corp., 208 A. 2d 61, 62 (Del. 1965) the court stated: “Courts in nearly all jurisdictions which have faced this problem have applied the general rule that the indemnitee is not to be viewed as an insurer and have indicated that the indemnitee will not be protected against the consequences of his own negligence unless the agreement clearly and unequivocally requires it.”
demnification contracts to provide indemnification against damages resulting from the negligence or other fault of the indemnitee, and have construed indemnification agreements which appear to be very broad and all-inclusive in their language, as not including indemnification for damages arising from the negligence of the employees of the indemnitee.\footnote{See McKenna and Bartler, \textit{Developments in the Law of Indemnity}, \textit{The Forum} Vol. 1 No. 1, p.7 (1965). Agreements to indemnify are to be strictly construed. \textit{Id.} at p.8. But for a modern, though still minority view, see Jacksonville Terminal Co. v. Railway Express Agency, Inc., 296 F. 2d 255, 261-62 (5th Cir. 1961).}

\footnote{4 See Curtis, \textit{Third-Party Indemnity and Coverage}, 1965 Ins. L.J. 594. The author states at p.594:

"No one should be permitted to benefit unjustly from his own wrongdoing. The active primary wrongdoer should ultimately bear the burden of damages and hold harmless the party who is a passive or technical tort feasor."

Also at p. 595:

"The decisional difficulty, however, is experienced in the constant battle as to who is to be considered passively negligent, and who, as a matter of law, is actively negligent. For this reason, if for no other, when the contract does not provide for absolute indemnity many opinions of divergent conclusions have been written."

See George Sollitt Constr. Co. v. Gateway Erectors, Inc., 260 F. 2d 165 (7th Cir. 1958) (negligence of the general contractor not expressly covered in contract of indemnity; courts require the language to be in explicit terms before enforcing indemnity); Whirlpool Corp. v. Morse, 222 F. Supp. 645 (D. Minn. 1963) (contract to hold party harmless even in event of its own negligence does not contravene public policy; case also describes the situations in which recovery may be had); Hollingsworth v. Chrysler Corp., 208 A. 2d 61 (Del. 1965).

See Ryan Stevedoring Co. v. Pan-Atlantic Steamship Corp., 350 U.S. 124 (1956) in which there was no express agreement of indemnity, but there was an informal agreement between shipowner and stevedore-contractor (Ryan) whereby the latter agreed to perform all owner's stevedoring operations. The owner of the ship was held liable for the injuries suffered by a longshoreman. Owner sued contractor, who had undertaken to do the owner's loading of the ship. The injuries were due to insufficiently secured rolls loaded by an employee of the contractor. The Court held that the shipowner had a right to indemnity from the contractor. The obligation is based upon what the Court termed the implied obligation of stevedore not only to stow the paper rolls, but to stow them properly and safely; the obligation is not "quasi-contractual" or "implied in law" or "arising out of a non-contractual relationship"; rather, the Supreme Court says, the obligation is "the essence of petitioner's stevedoring contract" and based upon a "warranty of workmanlike service that is comparable to a manufacturer's warranty of the soundness of its manufactured product." The Court stated (at p. 132) that "if the shipowner did hold such an express agreement of indemnity here, it is not disputed that it would be enforceable against the indemnitee." The contractor argued that the shipowner had an obligation to supervise and since he failed to do so, he should be barred from indemnity. But the Court said (at pp. 134-35):

"Whatever may have been the respective obligations of the stevedoring contractor and of the shipowner to the injured longshoreman for proper stowage of the cargo, it is clear that, as between themselves, the contractor, as the warrantor of its own services cannot use the shipowner's failure to discover and correct the contractor's own breach of warranty as a defense. Respondent's failure to discover and correct petitioner's own breach of contract cannot here excuse that breach." (Emphasis added.) See also Mayer v. Fairlawn Jewish Center, 38 N.J. 549, 186 A. 2d 274 (1962) where the court cited the \textit{Ryan} doctrine of implied contractual indemnity in a construction contract case. See also McKenna and Bartler, \textit{supra} note 3, at pp. 11 \textit{et seq.}, especially at pp. 15-18 for cases citing the \textit{Ryan} rule. These cases of implied contractual indemnity (\textit{i.e.}, related to a contractual relationship but...}
The Wisconsin Supreme Court recently held that the indemnity clause there involved was not applicable, because it did not expressly provide for indemnification for negligence solely caused by the alleged indemnitee. The Court stated it favored "strict construction of indemnity contracts" in line with "the overwhelming majority of the other states." The language of the indemnification contract in that case was broad, providing that the indemnitee (a subcontractor) would assume full responsibility for any damages to personal property "in the performance of the contract arising out of the assumed work, whether directly or indirectly, to be performed" by the indemnitee. The agreement also provided that the indemnitee would hold the owner and contractor harmless from any claims for injury "resulting from, or arising out of, and in connection with, any of the subcontractor's operations." In the light of this case, what are the drafting problems confronting the Wisconsin attorney preparing an indemnity clause to protect his owner-client? Similarly, what are the exposures undertaken by the contractor or lessee which its attorney should recognize and suggest insuring against?

**SEVEN POSSIBLE SITUATIONS TO BE CONSIDERED**

There are seven possible situations to be considered in connection with arriving at an indemnification agreement that will offer maximum protection to an owner seeking indemnification for any costs, expenses, damages, or the like, incurred as a result of operations by third parties (contractors, subcontractors, lessees, etc.) on its premises. These situations are:

1. The contractor or lessee is negligent and their negligence or other fault is the sole cause of the damages to person or property;
2. The contractor or lessee is negligent and the owner is also negligent, so that their combined fault is the sole cause of the damages;
3. Owner's negligence is the sole cause of damages.
4. The damages are caused by the negligence or other fault of some third party (i.e., a person who is not an employee, agent, or other legal representative of either the owner or the contractor or lessee);
5. The damages are caused by the fault of the owner and the fault of some third party;

without reference to an express indemnity provision) are beyond the scope of this article. Similarly, "common law indemnity" (i.e., without reference to a contractual relationship at all; see McKenna and Bartler, supra at pp. 20 et seq.) is also outside the scope of this article.

Mustas v. Inland Constr., Inc., 19 Wis. 2d 194, 120 N.W. 2d 95, 121 N.W. 2d 274 (1963).
Id. at 205.
Id. at 205.
Id. at 206.
Id. at 206.

Throughout this article, reference to fault of a contractor, lessee or owner should be read to include fault of any employee or other person for whose acts the contractor, lessee or owner is held legally responsible.
6. The damages are caused by the fault of the contractor or lessee and the fault of a third party;

7. The "accident" is a pure accident in that no one is at fault, but damages occur and the question of allocating the cost of these damages arises.

These various possible situations are discussed in the above order, in the following paragraphs:

(1) The law is well settled that any indemnification agreement will provide indemnification in cases where the damages arise solely from the fault or negligence of the contractor. If the owner incurs liability as a result of an accident so caused, there is, under the law of most jurisdictions, a common law right to indemnification which would be applicable even if no written indemnification agreement were present. "It is clear, from the foregoing common law rules that one who is himself without fault and is forced by operation of law to defend himself against the act of another, can recover over against that other the entire amount of the loss, including reasonable attorney's fees encountered."\(^{10}\) Accordingly, virtually any indemnification agreement worthy of its name will insure protection against expenses arising out of such an accident.

(2) In cases falling in the second category, the courts are reluctant to impose an obligation of indemnification upon a contractor in cases where the owner of the building, through negligence or other fault of its employees, contributed to the damages arising. Most courts have held that in such a situation the indemnification contract does not apply, unless there is an express statement that it is to be applicable to such a case or unless the court considers the language so clear that it admits of no other interpretation.

A number of factors have been considered by the courts in determining whether or not to enforce an indemnification agreement in such a situation. For example, in a Wisconsin case, *Criswell v. Seaman Body Corp.*,\(^{11}\) the owner of a building was held liable to an employee of a subcontractor for failure to comply with the Wisconsin Safe-Place Statute requirement to provide a "safe place" of employment, even though there was no active negligence or fault on the part of the owner. In a subsequent case involving the same accident, *Hartford Accident & Indemnity Co. v. Worden-Allen Co.*,\(^{12}\) in which the owner's insurer sued for indemnification for the amounts it had paid to the subcontractor's employee, the Wisconsin Supreme Court enforced indemnification against the subcontractor whose active negligence caused the


\(^{11}\) 233 Wis. 606, 290 N.W. 177 (1940).

\(^{12}\) 238 Wis. 124, 297 N.W. 436 (1941).
accident, although the contract did not state it applied where owner's fault contributed to the damages.\textsuperscript{13} The court expressed reservations as to whether the agreement would have applied had the accident been caused \textit{solely} by the active negligence of the owner.\textsuperscript{14} This distinction between active and passive negligence is commented on in \textit{Mustas v. Inland Const., Inc.}.\textsuperscript{15}

(3) In situations where the fault of the owner is the sole cause of the injuries, the courts are even more reluctant to impose liability upon the indemnitee. Typical of this attitude is the language of a federal court of appeals in \textit{Batson-Cook Co. v. Industrial Steel Erectors}.\textsuperscript{16} There the court stated that the imposition of such liability upon an indemnitee "must be spelled out in unmistakable terms. It cannot come from reading into the general words used the fullest meaning which lexicography would permit."\textsuperscript{17} The language of the indemnification agreement was very broad, stating that the building subcontractor would indemnify the general contractor for "any and all losses 'sustained in connection with or [alleged] to have arisen out of or resulting from the performance of the work by subcontractor. . . .'"\textsuperscript{18} A few courts have construed indemnification agreements to cover such a situation even though the language did not expressly cover a case where the owner-indemnitee was, or was claimed to be, negligent.\textsuperscript{19}
INDEMNIFICATION CONTRACTS

While there was much doubt in the early decisions, the modern cases are almost unanimous in holding that a contract which does expressly cover negligence of the indemnitee, is valid and will be enforced. An automobile and other liability insurance policies are examples of the same kind of contract. An obvious distinction exists between such indemnification contracts, and so-called exculpatory contracts whereby a contracting party signs away in advance any right to recover for damages incurred through the negligence or other fault of the other party to the contract. The latter contracts are still void in many states, and apparently in Wisconsin. An indemnity contract, on the other hand, does not prevent recovery for the damages; it merely shifts the burden of paying the damage to the indemnitee.

There are obvious problems in securing agreement to an indemnification contract that provides the contractor or lessee will have to pay for damages incurred even as a result of negligence of the owner. The dilemma is that unless the contract is drawn expressly so to provide, it probably will not be construed by a court to provide the desired indemnity in this situation.

(4) If the expenses and damages are incurred solely as a result of

both the indemnitee Railroad and the indemnitee Railroad are concurrently negligent. We hold that it does not."

The Court indicates the only situation where indemnity to the railroad would serve any purpose is in a case founded in whole or in part upon the railroad's own negligence.

One author has expressed the view that the general rule today no longer requires express mention of negligence of the indemnitee in order for the indemnity to apply.

"However, as time passed the courts have gradually realized (sic. relaxed) this rule so that no longer need the indemnification for one's own negligence be express or explicit as long as the intent is clear and unambiguous."


21 Jacksonville Terminal Co. v. Railway Express Agency, Inc., 296 F. 2d 256 (5th Cir. 1961). In Jacksonville, the court stated at p. 262:

"It presumes, first of all, that one party's assumption of liability for losses due to another's negligence is an 'unusual' and 'hazardous' undertaking. We cannot agree. In the light of modern conditions, we perceive little justification for so characterizing the indemnitor's obligation. Insurance companies assume this obligation every day . . . ."

the negligence or other fault of a third party (neither the contractor nor the owner) and if the incident meets the other tests of the indemnification language as to time (e.g., "during the time the contractor is performing work or is maintaining equipment on the premises"), place (e.g., "in or about the premises which are the subject of the contract"), and cause of occurrence (e.g., "arising out of or related to the contractor's operations"), the situation should be covered by the indemnification agreement. For example, the owner of a building might well incur liability under a workmen's compensation statute which would make the owner responsible for injuries incurred by one of his workmen on the premises, even though neither the owner nor the contractor were in any way at fault and the accident was caused solely by the fault of some third party or by the fault of the injured party himself. An indemnification agreement in the form commonly used should provide indemnification against such expenses.

(5) Where the owner's employees' negligence, together with negligence of a third party, contributes to causing the damages, the reluctance of the courts to broadly interpret an indemnification agreement comes into play again. Unless the agreement expressly says it is to apply even where the owner's fault causes or contributes to the damages, it will probably not provide indemnification. The cases do not generally distinguish these various situations, but merely express the rule that where the indemnitee's employees' fault contributes to the damages, express language is necessary for the agreement to apply. However, the courts probably would be most reluctant to apply an indemnification agreement where the sole fault is that of the owner's employees (situation 3), somewhat less reluctant where fault of some third party combines with owner's negligence (situation 5), and even less reluctant where owner's fault and the contractor-indemnitor's fault combine to cause the loss (situation 2). But in any of these situations the risk is substantial that no indemnification will apply unless the clause, in express and unambiguous terms, states it applies whether the owner is negligent or not.

(6) Where negligence of the contractor's employees combines with fault of a third party, indemnification would probably be applied under most indemnity clauses. Since no fault exists on the owner's part, the indemnity would probably be enforced even under the usual policy of strict interpretation.

(7) If the damages and costs incurred are a result of a pure accident which occurs during the time the contractor-indemnitor is on the premises and has some connection with the work of the contractor-indemnitor, most indemnification agreements would provide protection to

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the owner. An example of an instance where the owner of the building might incur expense in such a situation is under a workmen's compensation statute where liability could be incurred regardless of whether anyone was at fault.

**Drafting Problems**

A complicating factor in drafting indemnification contracts is that ultimate determination of fault is seldom made. That is to say, most claims are disposed of by settlement based on compromise and a weighing of the chances of liability being assessed against one or more alleged tortfeasors. The claimant may claim owner was at fault, but owner disagrees and contends the contractor's employee was negligent; the contractor may disagree with both and claim no one was at fault, or point to a third person or claimant himself as having caused the accident. Often there is also dispute whether the claim, in fact, "arose out of" or was "related to" the performance of the contract. To obviate this problem, indemnification clauses should contain language referring both to ultimate facts (e.g., "claims arising out of the contract") and to the "facts" as alleged by a claimant (e.g., or "claims alleged to arise out of the contract"). Similar references can be made regarding the fault question (e.g., "whether or not caused, or claimed to be caused, in whole or in part, by negligence or other fault of the owner.")

Two alternative forms of broad indemnification agreements are presented in Exhibits A and B. They are designed for a construction contract situation, but could be modified for use in lessor-lessee agreements. Exhibit A is a broad form of indemnification which would probably be construed by a court to provide indemnification protection to the "owner" in all of the seven situations discussed above. In order to provide this protection it is necessary that the language of the agreement be extremely explicit and detailed. This obviously may raise problems of the acceptability of such an agreement to contractors. Exhibit A is proffered, not as an example of a practical solution to the dilemma, but as an example of (1) the extreme to which it appears necessary to go to obviate most questions of interpretation and (2) the consequent problems of acceptability. Exhibit B is a modified form of indemnification agreement which is shorter and perhaps more readily acceptable to a contractor. It is believed that either indemnification is broad enough to provide indemnification in any of the seven situations; but the less detailed and explicit Exhibit B could give rise to problems, such as questions as to place and time of occurrence.

**Conclusion**

The problem of allocating the cost of injuries and property damage incurred on premises during the time work is being performed by contractors and subcontractors, or during lessee operations, presents, at base, a question of insuring against the risks and of who buys the in-
The indemnification agreements in Exhibits A and B are submitted with the idea that they may have the advantage of being clear in their intention to provide very broad coverage. One problem with a general form of indemnification which does not make explicit whether it is to provide indemnification in cases where the owner's negligence allegedly causes or joins in causing the damages, is that there is likely to be double insurance coverage with consequent duplication of cost. The owner buys coverage because there is doubt as to whether the indemnification agreement would protect it in cases of its own alleged negligence. On the other hand, a court might construe even a general indemnification agreement to require that the contractor-indemnitor pay expenses arising out of contractor's operations and incurred due to negligence of the owner while the contractor is on the premises. For this reason the contractor's insurer may also charge a premium to cover this risk. Clarifying the agreement by expressly stating what is intended avoids duplicating insurance premium costs and also can avoid the cost of litigating what was intended by an ambiguous statement.

Draftsmen are confronted with the dilemma of specifying negligence and frightening off prospective contractors and lessees, or else not specifying negligence and thus providing an indemnitor with a good argument for denying indemnity if the indemnitee is (or can arguably be said to be) at fault. It appears from the cases that draftsmen have by and large tried to make the indemnity as broad as possible but have avoided mentioning fault. The problem will not go away, and litigation is quite likely in a close case involving such a clause. If the indemnitee expects protection against liability for his own fault, it can reasonably be contended that the time has come to meet the issue squarely by having the contract expressly provide such protection. There is, after all, nothing immoral about insuring against liability for one's fault; the propriety is not diminished because the indemnitee happens to be a landowner instead of a motorist, and the indemnitor a contractor or lessee instead of an insurance company.

In any event there is no answer written bold in the sky as to who is at fault in these cases. Unless a broad indemnity clause is set up in the contract to include fault (or, more realistically, claimed fault) of the indemnitee, a dispute and litigation are likely. Consideration of the following exhibits or of similar indemnity clauses specifying what is

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24 For discussion of insuring against liability under indemnity contracts, see article by Curtis, supra note 19 at pp. 270-271. The author notes that most general liability policies exclude coverage of liability incurred under a contract, so that a special endorsement to provide such coverage is necessary. The attached specimen indemnity agreements contemplate that indemnitor will buy the insurance, and indemnitee is entitled to pass on the insurer selected and is to receive prior notice of any cancellation of policies.
intended in cases of fault of an indemnitee, might decrease the litigation in the field.

**Exhibit A**

The Contractor shall save and hold the Owner harmless from and against all liability, damage, loss, claims, demands and actions of any nature whatsoever which arise out of or are connected with, or are claimed to arise out of or be connected with, any of the work done by the Contractor, or its agents, servants, subcontractors or employees, or which arise out of or are connected with, or are claimed to arise out of or be connected with any accident or occurrence which happens, or is alleged to have happened, in or about the place where such work is being performed or in the vicinity thereof (1) while the Contractor is performing its work, or (2) while any of the Contractor’s property, equipment, or personnel, are in or about such place or the vicinity thereof by reason of or as a result of the performance of Contractor’s work; including without limiting the generality of the foregoing, all liability, damages, loss, claims, demands and actions on account of personal injury, death or property loss to Owner, its employees, agents, subcontractors or frequenters, Contractor, its employees, agents, subcontractors or frequenters, or to any other persons, whether based upon, or claimed to be based upon, statutory (including, without limiting the generality of the foregoing, workmen’s compensation), contractual, tort, or other liability of Owner, Contractor, or any other persons, and whether or not caused or claimed to have been caused by active or inactive negligence or other breach of duty by Owner, its employees, agents, subcontractors or frequenters, Contractor, its employees, agents, subcontractors or frequenters, or any other person. Without limiting the generality of the foregoing, the liability, damage, loss, claims, demands and actions indemnified against shall include all liability, damage, loss, claims, demands and actions for trade-mark, copyright or patent infringement, for unfair competition or infringement of any other so-called “intangible” property right, for defamation, false arrest, malicious prosecution or any other infringement of personal or property rights of any kind whatever.

The Contractor shall at its own expense investigate all such claims and demands, attend to their settlement or other disposition, defend all action based thereon and pay all charges of attorneys and all other costs and expenses of any kind arising from any such liability, damage, loss, claims, demands and actions. The Contractor shall secure, at its own cost and expense, insurance, in amounts and with a company acceptable to and approved by the Owner, against the liability assumed in this paragraph by the Contractor. The Contractor shall furnish the Owner certificates of the insurance company as to the particulars of such insurance coverage. The insurance policies shall provide that all
notices by the insurer to the insured shall simultaneously be given to the Owner, that at least ten (10) days prior to any cancellation of such policies notice in writing shall be given to the Owner, and that unless such notice is given the purported cancellation will be ineffective.

**Exhibit B**

The Contractor shall save and hold the Owner harmless from and against all liability, claims and demands on account of personal injuries (including, without limitation of the foregoing, workmen's compensation and death claims) or property loss or damage of any kind whatsoever, which arise out of or are in any manner connected with, or are claimed to arise out of or be in any manner connected with, the performance of this contract, regardless of whether such injury, loss or damage shall be caused by, or be claimed to be caused by, the negligence or other fault (a) of Contractor, or (b) of a subcontractor hereunder, or (c) of Owner, or (d) of some other person; or by any agents or employees of any of the foregoing; or by accident; or otherwise.25

[Include also second paragraph similar to second paragraph of Exhibit A.]

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25 See Aluminum Co. of America v. Hully, 200 F. 2d 257 (8th Cir. 1952) for a similar clause.