



Insurance Coverage:

An Overview and Update
on Anti-Indemnity Statutes

Indemnification

What it is...

- A risk shifting mechanism
- One party's promise to protect another party from any loss
- A common provision in commercial contracts

Indemnification

Example from a software vendor service agreement:

limited to) patent, copyright, trademark, servicemark and trade secret rights, shall remain with and be owned exclusively by [REDACTED] and/or its suppliers or licensors.

(b) **Indemnification.** Customer shall indemnify and hold [REDACTED] and/or its licensors and suppliers harmless against any and all liability (including any costs, fees and expenses of attorneys, collection agencies and others, any and all damages, judgments or other claims and losses) incurred by [REDACTED] (collectively "Damages")) relating to or arising out of Customer's:

- (i) unauthorized use (including reverse engineering), disclosure or dissemination of the Software and third parties' confidential material
- (ii) violation of [REDACTED]'s or any third party's intellectual property rights
- (iii) breach of the terms of any related license, support, supply or other Agreement as identified in Appendix B.

8. CUSTOMER OBLIGATIONS

Customer must, at all times, comply with the following requirements:

Indemnification

It's not always fair

- Superior bargaining power = benefit of indemnification
- It can be a “bully’s tool”



Indemnification

Example:

Small software vendor – “SmallSoft”

Big university customer – “Big U”

\$10,000 contract with a promise of more (“this is the start of big things!”)

Big U insists on indemnification in its favor

Third-party lawsuit for data breach

Legal fees: \$48,000

Settlement: \$120,000 (actual loss and identity monitoring)

Indemnification

The legislative solution? Anti-indemnity statutes.

THE “IF ... THEN” GAME

- IF the loss is an anti-Indemnity jurisdiction...
... THEN contractual indemnity may be void.
- IF the contractual indemnity is void...
... THEN there is no coverage for “Insured Contracts.”
- IF there is no additional insured issue...
... THEN there is no coverage for the loss.

A Patchwork of Laws

- Some states prohibit indemnity for sole negligence only
- Some states prohibit indemnity for sole or partial negligence
- Some states also prohibit additional insured provisions
- Some states do nothing at all



Roadmap



- Anti-indemnification statutes: what they prohibit and how the caselaw has affected the landscape
- Insured contracts
- Addition insureds: the loophole around the prohibitions
- How to incorporate this into your approach to claims

Example

- You receive notice of a claim from an Oklahoma company who is sued by the employee of your insured Kansas subcontractor.
- Your insured agreed to indemnify the Oklahoma company for all losses on the project.
- Finally, the Oklahoma company is also additional insured on the policy.
- Is there coverage?

ANTI-INDEMNITY ACTS



Three Approaches:

Approach #1: Sole Negligence

- Parties can agree to indemnity, but the provision will not be enforced if the indemnitee is 100% negligent
- Practically, sole negligence does not get sorted out until the jury apportions liability. You are going to trial.

Three Approaches:

Approach #2: Sole and Partial Negligence

- Indemnitor can only indemnify indemnitee for indemnitor's negligence
- Reasoning:
 - Protects non-negligent parties from the recklessness of others; i.e., it might cause indemnitees to be less careful if they know that someone else is footing the bill
 - Actively trying to protect parties with weaker bargaining positions
- Practical application: The indemnitee's carrier will be paying for its own defense

Three Approaches:

Approach #3: No Express Prohibition

- Legislature has not addressed it
- Caselaw still shapes indemnity provisions

In Pennsylvania...

In *Ruzzi*, the owners of a gas station hired a contractor to, among other things, supply and install gasoline tanks at their station. In the parties' contract, the station owners agreed to [*248] indemnify the contractor "from any and all claims for loss, damage, injury [***6] or other casualty . . . caused or occasioned by any . . . explosion . . . occurring . . . by reason of the . . . installation and/or repair of" the tanks. 588 A.2d at 3. When one of the tanks to be installed arrived at the site with a hole, a resulting explosion injured a third party who had been hired by the contractor. The contractor was found to be 84% negligent and sought indemnity from the gas station owners pursuant to the contract. In spite of the broad language in the indemnity provision, this Court held that the agreement did not provide indemnity to the contractor for its own negligence, reaffirming the rule previously announced in *Perry v. Payne*, 217 Pa. 252, 66 A. 553 (Pa. 1907), that HN1 "if parties intend to include within the scope of their indemnity agreement a provision that covers losses due to the indemnitee's own negligence, they must do so in clear and unequivocal language. No inference from words of general import can establish such indemnification." 588 A.2d at 4. As the *Ruzzi* court explained, assuming liability for the negligence of an indemnified party "is so hazardous, and the character of the indemnity so unusual [***7] and extraordinary, that there can be no presumption that the indemnitor [***379] intended to assume the responsibility unless the contract puts it beyond doubt by express stipulation." *Id.* (quoting *Perry*, 66 A. at 557). Moreover, as this Court noted in *Perry*, it would be "contrary to experience and against reason" for a contractor to agree to indemnify another for the other's negligence, when such indemnification would subject it to "uncertain and indefinite" liability. *Perry*, 66 A. at 555.

“INSURED CONTRACT”

CONTRACT

Insured Contract

- A defined term common in liability policies
- States that the standard exclusion for contractually assumed liability does not apply to liability assumed in an "insured contract."
- In most cases this provides coverage for liabilities assumed in an enforceable indemnity provision of a commercial contract.

Insured Contract

Sample Exclusion:

b. Contractual Liability

"Bodily injury" or "property damage" for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement. This exclusion does not apply to liability for damages:

- (1) That the insured would have in the absence of the contract or agreement; or
- (2) Assumed in a contract or agreement that is an "insured contract", provided the "bodily injury" or "property damage" occurs subsequent to the execution of the contract or agreement. Solely for the purposes of liability assumed in an "insured contract", reasonable attorney fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be damages because of "bodily injury" or "property damage", provided:
 - (a) Liability to such party for, or for the cost of, that party's defense has also been assumed in the same "insured contract"; and
 - (b) Such attorney fees and litigation expenses are for defense of that party against a civil or alternative dispute resolution proceeding in which damages to which this insurance applies are alleged.

Insured Contract

Sample Definition:

9. "Insured contract" means:
- a. A contract for a lease of premises. However, that portion of the contract for a lease of premises that indemnifies any person or organization for damage by fire to premises while rented to you or temporarily occupied by you with permission of the owner is not an "insured contract";
 - b. A sidetrack agreement;
 - c. Any easement or license agreement, except in connection with construction or demolition operations on or within 50 feet of a railroad;
 - d. An obligation, as required by ordinance, to indemnify a municipality, except in connection with work for a municipality;
 - e. An elevator maintenance agreement;
 - f. That part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.

Insured Contract

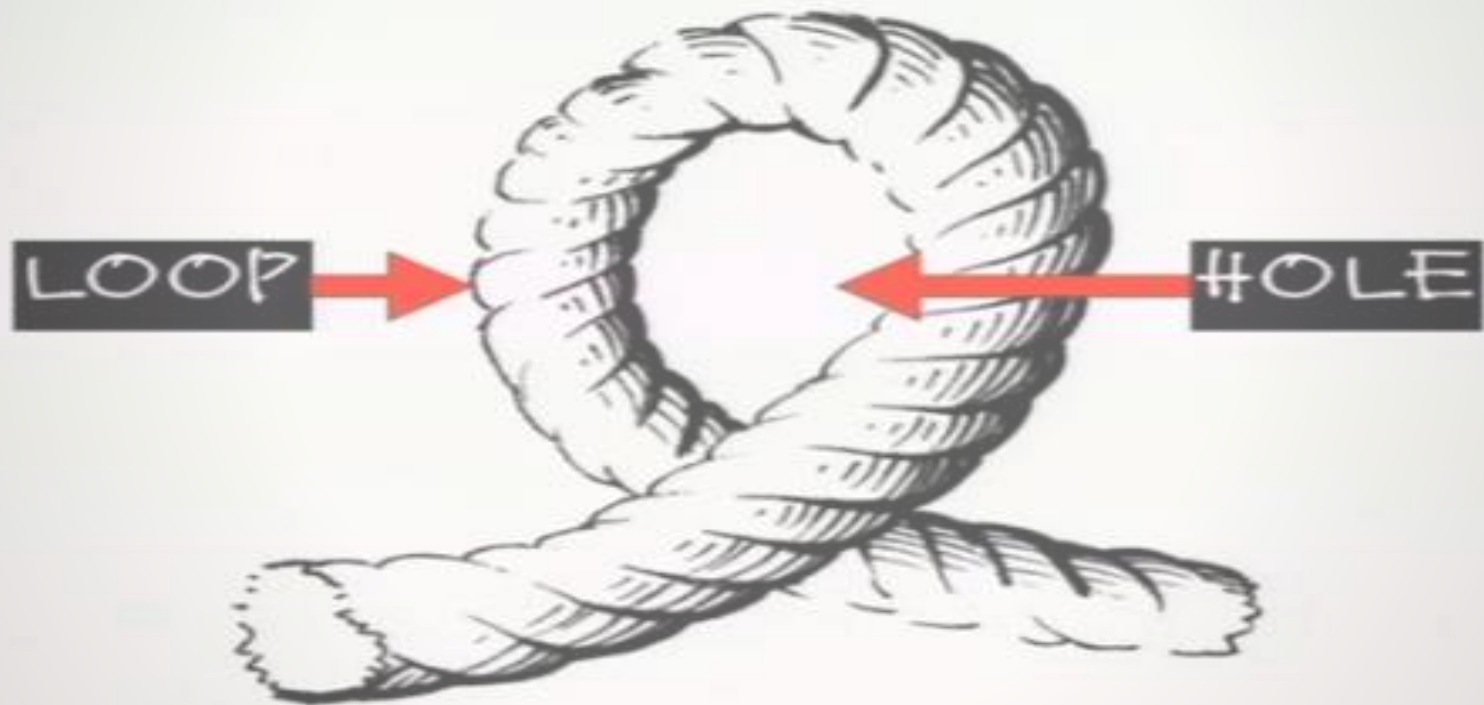
How does this play out?

- Sole Negligence Jurisdiction
 - The indemnity provision will only be enforced if the indemnitee is **not** 100% negligent
 - You're going to trial with a reservation of rights in place
- Sole or Partial Negligence Jurisdiction
 - You will only be covering liability caused by your insured, the indemnitor

Insured Contract

- No Statute
 - You will cover the indemnitee's negligence in addition to your insured's negligence, so long as the indemnity provision is properly drafted
 - A court can decide the enforceability of the provision as a matter of law
 - Paradoxically, in jurisdictions like PA you can actually have a determination of this before you would in the other jurisdictions

THE ADDITIONAL INSURED LOOPHOLE



Additional Insured Loophole

- Some commercial contracts required the indemnitor to also obtain insurance coverage for the indemnitee

Example:

§ 11.1.4 The Contractor shall cause the commercial liability coverage required by the Contract Documents to include (1) the Construction Manager, the Construction Manager's consultants, the Owner, the Architect, and the Architect's consultants as **additional insureds** for claims caused in whole or in part by the Contractor's negligent acts or omissions during the Contractor's operations; and (2) the Owner as an **additional insured** for claims caused in whole or in part by the Contractor's negligent acts or omissions during the Contractor's completed operations.

Additional Insured Loophole

- Anti-indemnity acts do not apply to the insurance contract itself in almost every jurisdiction
- Exceptions:
 1. Colorado
 2. Georgia
 3. Montana
 4. Oklahoma
 5. Oregon
 6. Texas

INCORPORATION INTO YOUR APPROACH TO CLAIMS

Claims Application

- Determine the jurisdiction of the loss, or at least the universe of states' laws that could apply
- Resolve choice of law questions, if necessary
- Determine the type of jurisdiction for the controlling law: sole negligence, sole or partial negligence, or no statute
- Determine if there is an additional insured issue and whether the controlling jurisdiction forbids additional insured provisions

Claims Application

- **Examples**

1. If your insured agreed to indemnify another party in a sole negligence state and the other party's sole liability has already been determined, there's no coverage. End of the inquiry.
2. If the indemnitee is also an additional insured in a jurisdiction that does not prohibit such practices, you must provide a defense.

Solve the Problem

- You receive notice of a claim from an Oklahoma company who is sued by the employee of your insured Kansas subcontractor.
- Your insured agreed to indemnify the Oklahoma company for all losses on the project.
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QUESTIONS?