

CONTRACT LIABILITY LANGUAGE FOR THE RISK MANAGER



Brought to you by the Risk and Insurance Management Society of Pittsburgh and the Law Offices of Wayman, Irvin & McAuley, LLC

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Contractual Liability Language

- Goal: Limit the amount of exposure to the company
- How: By passing the risk off to the other contracting party

The Risk Manager and The Contract

With every contract, the risk manager should:

1. Read through the contract
2. Evaluate the risks in the contract and the clauses associated with risk
3. If you cannot obtain agreeable language, rely on counsel
4. Maintain a file of all contractual agreement for twelve years
5. Keep communication lines open

Three Means to Control Liability Through Contracts

1. Indemnification clause
2. Additional insured clause
3. Hold Harmless/Limitation of Liability clause

INDEMNIFICATION

- Works two ways:
 - Your company is indemnified by another for a loss
or
 - Or your company indemnifies another for a loss

INDEMNIFICATION

- Whether using form contracts or a specifically tailored contract, a risk manager must make sure that the contract contains an indemnity clause which obligates the other contracting party to indemnify the company against claims brought by third parties

INDEMNIFICATION

To enforce an indemnification provision, the contract must:

- Not contravene public policy
- Relate only to the contracting parties while excluding matters of public interest;
- Result from equal bargaining power; and,
- Clearly state the beneficiary being relieved of liability

Krueger Assocs. V. ADT Sec. Sys., 247 F.3d 61 (3d. Cir. 2001)

INDEMNIFICATION

- An entity can be indemnified for its own negligence. *DiPeietro v. City of Philadelphia*, 496 A.2d 407 (Pa. Super. 1985) & *Westinghouse Elec. Co. v. Murphy, Inc.*, 228 A.2d 656 (Pa. 1967)
- However, such an indemnity clause **MUST** be clear and unequivocal that the other contracting party is providing indemnification for the others own negligence

INDEMNIFICATION

Perry-Ruzzi Rule

- *Perry v. Payne*, 66 A. 553 (Pa. 1907) held “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.”

INDEMNIFICATION

Perry-Ruzzi Rule

- *Ruzzi v. Butler Petroleum Co.*, 588 A.2d 1 (Pa. 1991) held “assuming liability for the negligence of an indemnified party is so hazardous, and the character of the indemnity so unusual and extraordinary, that there can be no presumption that the indemnitor intended to assume the responsibility unless the contract puts it beyond doubt by express stipulation.”

INDEMNIFICATION

Perry-Ruzzi Rule

- *Greer v. City of Philadelphia*, 795 A.2d 376 (Pa. 2002), contract that states “...subcontractor agrees to indemnify and hold harmless owner and contractor from and against claims...arising out of or resulting from the performance of the subcontractor’s work under this subcontract...but only to the extent caused in whole or in part by negligent acts or omissions of the subcontractor...regardless of whether or not such claim...is caused by a party indemnified hereunder.”
- The Supreme Court found this language not clear and unequivocal because the language did not demonstrate an unambiguous intention to provide indemnification to damages attributed to the negligence of the contractor.

INDEMNIFICATION

Perry-Ruzzi Rule

- *Bush v. Chicago & Northwestern Trans. Corp.*, 522 F.Supp. 585 (E.D. Pa. 1981), the found this language, “Shipper hereby releases and agrees to indemnify and save CSX harmless for all penalties, taxes...damage, loss, and liability arising directly or indirectly out of the ...use...or operation of the trailer from any cause” does not contain the necessary unequivocal terms necessary to indemnify for another’s negligence. It contains only words of general import.

INDEMNIFICATION

Perry-Ruzzi Rule

- *Morgan v. Harnischfeger Corp.*, 791 A.2d 1273 (Pa. Commw. 2002), the Court found this language, “Contractor shall assume the entire liability for an damage or injury of any kind or nature whatsoever to all persons ...and to all property caused by, resulting from, or arising out of the active or passive negligence of the owner...agrees to indemnify and hold harmless the owner from and against all claims...” sufficiently specific to enforce even for the owner’s negligence.

INDEMNIFICATION

Perry-Ruzzi Rule

- In *Urban Redevelopment Authority of Pittsburgh v. Noralco Corp.*, 422 A.2d 563 (Pa. Super. 1980), the Court found required indemnification because Noralco's contract required it to "indemnify and save harmless the URA from any claims or damages...to have been suffered while performing this contract" and no evidence demonstrated the owner was actively negligent.

INDEMNIFICATION

Perry-Ruzzi Rule

- In *Westinghouse Elec. Co. v. Murphy, Inc.*, 228 A.2d 656 (Pa. 1967), the Supreme Court examined indemnification language which stated: “Seller shall...indemnify and save harmless Buyer against and from any and all claims...and all other liabilities whatsoever on account of...suffered by Seller...whether the same results from negligence of Buyer or Seller from any and all loss by reason of the premises” and held that the Seller had to indemnify the Buyer for the underlying personal injury action

INDEMNIFICATION

Perry-Ruzzi Rule

- Under the *Perry-Ruzzi* rule, if a court has to decide whether a party is liable for the share of damages attributed by a jury to the negligence of the party seeking indemnity, the party seeking indemnity must establish the contract indemnity language is clear and unequivocal.

INDEMNIFICATION

- The indemnification clause should cover the company and the company's employees
- If the other contracting party enters into any subcontracts, make sure those contracts also contain indemnification clauses requiring indemnification of your company

Indemnification

Pass through provisions

Bernotas v. Super Fresh Food Markets, Inc., 863 A.2d 478 (Pa. 2004), the Court examined an incorporation clause between a contract of a general contractor and a subcontractor. The Plaintiff sustained injuries at a job site. The court found the general contractor had an obligation to indemnify the owner. The general contractor sought indemnification from the subcontractor.

Indemnification

Pass through provisions

Bernotas v. Super Fresh Food Markets, Inc., continued:

The Court's analysis focused on whether the incorporation clause between the general and the sub, which incorporated the contract between the general and the owner bound the sub to indemnify the owner. In essence, the sub's duty to indemnify the owner passed through the contract between the sub and the general.

Indemnification

Pass through provisions

Bernotas v. Super Fresh Food Markets, Inc., continued:

- Because the agreement between the general and the sub did not clearly express the parties intention regarding whether the sub would have to indemnify the general for the general's own negligence, the clause did not require indemnification.
- Unless expressly stated, pass through indemnification clauses violate the rule narrowly construing indemnification provisions.

INDEMNIFICATION

- Certain indemnity provisions are void as against public policy
 - *Fulmer v. Duquesne Light Co.*, 543 A.2d 1100 (Pa. Super. 1985)(Tortfeasor cannot sue Plaintiff's employer for indemnification when the Plaintiff sustained on the job injuries, unless liability for such damages is expressly provided for in a written contract, 77 P.S. § 481).
 - Pennsylvania does not allow a design professional to be indemnified for a loss caused by the design professionals negligent design documents (68 P.S. § 491)

INDEMNIFICATION

- Courts will construe indemnification provisions strictly and against the drafting party. *El v. SEPTA*, 297 F. Supp.2d 758 (E.D. Pa. 2003) & *Ratti v. Wheeling Pittsburgh Steel Corp.*, 758 A.2d 695 (Pa. Super. 2000).
- Courts will construe indemnification provisions to cover losses that are reasonably intended to be covered.

INDEMNIFICATION

- The Courts look to see if the indemnification clause insulates “all liability” or “all loss”
 - *Bush*, 522 F.Supp. 585 (E.D. Pa. 1981)(Examining when courts will refuse indemnification when the contract calls for indemnity from all liability, but permitting indemnification when the contract refers negligence and loss).
- The clause **MUST** include negligence

Indemnification Workers Compensation Act

- See Fulmer above
- In *Shumosky v. Lutheran Welfare Serv.*, 784 A.2d 196 (Pa. Commw. 2001), a contract between tortfeasor and plaintiff's employer only provided for indemnity in patients' action against the tortfeasor arising out of services provided and not related to work place injuries. The Workers' Compensation Act requires clear, unequivocal, and exact language. 77 P.S. § 481.

INDEMNIFICATION

- The Courts will not read the term “gross negligence” into an indemnity agreement where the agreement only uses the term negligence. *Ratti v. Wheeling Pittsburgh Steel Corp.*, 758 A.2d 695 (Pa. Super. 2000)
- The Pennsylvania Courts hold that a person who has secondary liability may recover indemnification from the party that has primary liability

INDEMNIFICATION

- Some jurisdictions have anti-indemnity statutes that vary in scope and breadth
 - North Carolina, via statute, precludes an agreement to indemnify against an entities own negligence is unenforceable
 - Texas: allows the enforcement of indemnity clause against an entities own negligence if the contract demonstrates that there is an intent to indemnify for the others own, active negligence

ADDITIONAL INSURED

- An additional insured clause requires the other contracting party to name your company as an insured under an existing insurance program
- These can minimize potential liability by creating an additional layer of insurance

ADDITIONAL INSURED

- When entering into a contract, ascertain whether the Company should be an additional insured under the other contracting party's insurance program
- If so, make sure the contract also requires that the other party's insurance is primary

ADDITIONAL INSURED

- When the contract requires a separate party to be an additional insured on your insurance program, review the entire insurance program to ensure that enough coverage exists and no exclusion would preclude coverage

ADDITIONAL INSURED

- It is also advisable to require the contracts to name your company as an additional insured on all policies held by subcontractors
- Make sure you secure the Certificate of Insurance from any entity that is supposed to name you as an additional insured

ADDITIONAL INSURED

- In *Harbor Ins. Co. v. Lewis*, 562 F.Supp. 800 (E.D. Pa. 1983), the Court held that an additional insured relationship was created through an endorsement of a policy, but cautioned that the endorsement did not provide blanket coverage, but was strictly tied to the actions of the named insured.

ADDITIONAL INSURED

Harbor Ins. Co. v. Lewis, con't

The additional insured endorsement stated:

- “It is agreed that the insurance afforded by this Policy shall apply to the following additional insureds but only to the extent of liability resulting from occurrences arising out of negligence of Reading Company and/or its subsidiaries:
City of Philadelphia”
- The additional insured was not entitled to coverage for its own negligence under the endorsement.

ADDITIONAL INSURED

Harbor Ins. Co. v. Lewis, con't

- The Court found that the policy was not an all risk policy covering the City because the insured was not charged an additional premium
- The Court examined the language of the policy, the language of the endorsement, the customary practices of the insurance industry regarding additional insured clauses, and the evidence of intent to conclude that no coverage existed.

ADDITIONAL INSURED

- In *Philadelphia Elec. Co. v. Nationwide Mut. Ins. Co.*, 721 F.Supp. 740 (E.D. Pa. 1989), Plaintiff filed a declaratory judgment action seeking indemnification because it was an additional insured pursuant to an endorsement.
- The endorsement stated that the applicable language of who was an insured was found in the Certificate of Insurance

ADDITIONAL INSURED

- The Certificate of Insurance stated:
“Philadelphia Electric Company...are added as Additional Insureds for any work performed by Contractor on their behalf.”
- Because the Certificate of Insurance limited the scope of coverage and the facts in the underlying Complaint plead that the Electric Company can only be held liable if it is found negligent by an act or omission on its part, then they are not additional insured under the policy because it was not the insured’s (contractor) work.

ADDITIONAL INSURED

- *Meridian Mut. Ins. Co. v. Continental Bus. Ctr.*, 2005 U.S. Dist. LEXIS 6406 (E.D. Pa. 2005), the Court analyzed a policy endorsement between a business and the office complex that leased the space to the business.

ADDITIONAL INSURED

- *Meridian Mut. Ins. Co. v. Continental Bus. Ctr.*, con't
 - The Endorsement stated: “any person or organization who you are required to name as an additional insured on this policy under a written contract or agreement.”
 - The Endorsement limited the additional insured’s coverage for claims arising out of real property owned, rented, leased, or occupied by the business.
- The lease between the business and the office complex required the business to list the office complex as an additional insured.

ADDITIONAL INSURED

- *Meridian Mut. Ins. Co. v. Continental Bus. Ctr.*, con't
- The Court held that the endorsement does not provide coverage because there is no allegation in the underlying complaints that the business was negligent or had anything to do with the business' property.
- Since no claim against the office complex arose from the property of the business, the office complex did not have a right to coverage

LIMITATION OF LIABILITY & HOLD HARMLESS

- The Third Circuit has upheld the enforceability of limitation of liability clauses
- Limitation of liability clauses are enforced under the Uniform Commercial Code involving the sale of goods when the parties are sophisticated and only economic losses are alleged

Limitation of Liability

- Be weary of entering into contracts that limits another's potential liability to you
- The Courts will, generally, uphold limitation of liability clauses if the parties are of equal sophistication

Limitation of Liability

- Contains four elements
 - The party who is benefiting from the limitation of its liability;
 - The party agreeing to limit its own recovery for someone else's negligence;
 - The type of claims to which the limitations apply; and,
 - The amount of the limitation

Limitation of Liability

- Element One: The Party Receiving the Benefit of the limitation
 - Clear language required
 - “Owner” or “Company” and its consultants, partners, employees, agents, subsidiaries shall not be liable”
 - The clause identifies who is not to be liable

Limitation of Liability

- Element Two: Party Agreeing to Limit Its Recovery
 - The “Owner” or “Company” ...shall not be liable to *(insert other contracting party’s name here)*
 - It only reduces the liability between the contracting parties, not third parties

Limitation of Liability

- Element Three: The Claims or Liabilities to Which the Limitation Applies
 - “....for any and all claims, losses, expenses, injuries, or damages arising out of or any way related to _____ or this Agreement by reason or any act or omission, including breach of contract or negligence not amounting to willful or intentional conduct...”
 - This clause covers direct claims from the other contracting party

Limitation of Liability

- Element Four: The Amount of Limitation
 - Examples
 - “Shall not exceed the amount of the contract”
 - “...shall not exceed \$_____”
 - “Shall not exceed the amount of the contract or \$_____, whichever is greater.”
 - “Shall be limited solely to the amount of available insurance coverage”

Limitation of Liability

- Enforceability
 - The law permits parties possessing relatively equal bargaining power to elect to limit the liability of one party to the other
 - The Clause must be conspicuous and clear

Limitation of Liability

- Trade offs
 - Increased costs to the party receiving the benefit of the limitation clause
 - If not properly drafted, the clause could be voided
 - May not protect against alleged willful, wanton, or gross negligence claims
 - May be void based on the particular jurisdiction's public policy

Hold Harmless

- A clause that states that one party will assume the risk of legal liability for the other party
- It obligates one party to pay any costs the other incurs as a result of a claim or lawsuit

Hold Harmless

- Participant Waivers
 - A type of hold harmless clause that organizations can use to protect itself from potential claims of participants in an activity or event
 - A person or entity must knowingly and voluntarily waive their rights
 - If it does not bar the suit, it certainly supports the assumption of the risk defense

DISCLAIMERS

- Is an express disavowal by one party to a transaction
- Disclaims differ from waivers in that they are unilateral
 - The injured party does not explicitly agree to the liability limitation
- The disclaimer may indicate that certain affirmative conduct will not incur
 - Thus disclaiming any duty to perform that conduct
 - An example is providing security at an event

Other Tips and Recommendations

- Always, always, always, have either an experienced risk manager, appropriate officer, or an attorney review the contract before it is signed
- Be weary of incorporation clauses that incorporate other or prior contracts

CONCLUSION

- Potential risks associated with entering into contracts can be minimized
- Requires careful reading of the contract and that certain clauses insulate your company from unpredictable exposure
- On the other hand, with such protection, the company must be prepared to pay more upfront because the other party is now assuming a risk