The State neither indemnifies nor defends its contractors

Indemnity

The term "indemnity" means "[a] duty to make good any loss, damage, or liability incurred by another." *Black's Law Dictionary* (9th ed. 2009). An "indemnity clause" is "[a] contractual provision in which one party agrees to answer for any specified or unspecified liability or harm that the other party might incur. — Also termed hold-harmless clause; save-harmless clause." *Id.*[1]

For nearly fifty years, South Carolina's attorneys general have consistently opined that state agencies have no authority to enter into indemnity or "hold harmless" agreements.[2] In fact, the Attorney General has even advised against the use of qualifying language – *e.g.*, "so far as the laws of the State permit" or "insofar as it lawfully may" – on the grounds that such language does not validate otherwise illegal indemnity obligations. *Id.*

Clauses that create an indemnity are not always obvious. No specific language or "magic words" are required to support indemnification, and a written agreement can be established without specifically expressing the obligation as indemnification.[3] An indemnification agreement is created when the words used express an intention by one party to reimburse or hold the other party harmless for any loss, damage, or liability.[4] A indemnity agreement can exist even when not described as indemnification.[5]

To illustrate language creating an indemnity obligation, consider this classic example appearing in form construction contracts:

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[1] In most instances, an indemnity agreement is any promise to pay another party for a loss or damage that party incurs to a third party. *Laurens Emergency Med. Specialists, PA v. M.S. Bailey & Sons Bankers*, 584 S.E.2d 375, 377 (2003) ("[T]he default rule of interpretation for indemnity clauses is that third party claims are a prerequisite to indemnification."). Nevertheless, the language used to craft "an indemnify clause [may] provide for other forms of compensation, including one in which a first party is liable to a second party for a loss or damage the second party might incur." *Id.*

[2] *Letter to Wayne F. Rush*, S. C. Att'y Gen. Op. of September 29, 2004.

[3] *McNally & Nimergood v. Neumann-Kiewit Constructors, Inc.*, 648 N.W.2d 564, 570 (Iowa 2002). *See, also, Royal Ins. Co. of Am. v. Whitaker Contracting Corp.*, 242 F.3d 1035, 1041 (11th Cir.2001) (particular language not required as long as intent is clear).

[4] Robert L. Meyers III & Debra A. Perelman, Symposium, *Risk Allocation through Indemnity Obligations in Construction Contracts*, 40 S.C. L.Rev. 989, 990 (1989).

[5] 41 Am. Jur. 2d, *Indemnity* § 7.

> … Contractor shall indemnify and hold harmless the Owner, Architect, Architect's consultants, and agents and employees of any of them from and against claims, damages, losses and expenses, including but not limited to attorneys' fees, arising out of or resulting from performance of the Work ….

AIA Document A201-1997, General Conditions of the Contract for Construction, Article 3.18.1. Unfortunately, contracts are not always so clear. Suppose the agreement provided for a contractor's indemnity, as above, then listed specific circumstances where the indemnity obligation did not obtain. Suppose the list were followed by a sentence reading "Owner shall be responsible for any costs or damages that result from any of these causes." Does this language create an obligation for the owner to indemnify the contractor for the excepted circumstances?

Now consider a provision that the owner is responsible for claims arising from his use of the project during construction. Does language that "Owner must pay any judgment resulting from such claims" mean just that he is on his own? Or does it mean he will pay any judgment, *including one against the contractor*, resulting from the owner's activities on the jobsite?

Rules requiring clear and unequivocal language to impose an indemnity obligation may resolve the cases above in the owner's favor.[6] The better practice, though, is not to risk it. If you see a provision obligating the state or an agency to pay a judgment, make sure it cannot be construed as an indemnity. If you aren't sure, add language to remove any ambiguity. For example, you may add the following phrase after an unclear sentence: "provided that nothing in this section creates any obligation for owner to hold contractor harmless from, or defend contractor against, such claims."

Defense

Closely related to indemnity is a duty to defend. "A duty to defend is a 'specific obligation to assume, upon tender, the defense obligations and costs of another.'"[7]

A duty to defend may be expressly stated, or it may be implied in a broad "save harmless" provision; an agreement to hold another harmless "from any and all loss, cost, or

[6] For example, in the absence of a legal duty a contractual promise to hold harmless "should not be found unless it can be clearly implied from the language and purpose of the entire agreement and the surrounding facts and circumstances." 41 Am. Jur. 2d, Indemnity § 7.

[7] MT Builders, L.L.C. v. Fisher Roofing, Inc., 197 P.3d 758 (Ariz. App. Div. 1 2008) (quoting Steven G.M. Stein & Shorge K. Sato, *Advanced Analysis of Contract Risk-Shifting Provisions: Is Indemnity Still Relevant?*, 27 Construction Lawyer 5, 9 (Fall 2007)). *See, generally*, *Crawford v. Weather Shield Mfg.*, 38 Cal. Rptr. 3d 787, 806 (Cal. Ct. App. 2006), *aff'd*, 187 P.3d 424 (2008) ("A defense obligation is of necessity a current obligation. The idea is to mount it, render it, and fund it now, before the insured's-or indemnitee's-default is taken, or trial preparation is compromised.").

expense" probably means you may be obligated to pay for his lawyer as well as any judgment he suffers when the lawyer settles or loses the case.

For many of the same reasons state agencies lack authority to indemnify, the Attorney General has opined that a governmental entity may not agree to defend a contractor against claims. This prohibition applies even where the claims arise from the government's own acts or omissions.[8]

Fortunately, defense clauses are easy to spot. They are most often stated in, or implied from, broad indemnity provisions, like the one quoted above. Or, they may stand alone as a separate clause or sentence within the overall indemnity section. In the latter case, look for language like "defend and indemnify" or "including attorney's fees."

Notification of a claim usually triggers a duty to defend. If the contractor is obligated to give you notice of claims, keep looking. There's probably a duty to defend lurking. If you aren't sure, the disclaimer phrase at the end of the Indemnity section, above, should catch any hidden or implied duty to defend.

Tips

□ Remove any clause that clearly creates any obligation for the government to indemnify anyone. Likewise, remove any language that expresses an intention by the government to reimburse or pay the other party for any loss, damage, liability, or judgment.

□ Take the same approach to language that requires you to provide a defense against claims, or to save harmless from costs, or attorney's fees, or expenses of suit.

□ If you suspect that a clause imposes an indemnity obligation on the government and you cannot get the contractor to remove the language, add clarifying language to the offending sentence. Use a phrase like this one: "provided that nothing in this section creates any obligation for the State to hold contractor harmless from, or defend contractor against, such claims."

[8] *Letter to John. J. Fantry, Jr.*, S.C. Att'y Gen. Op. of March 6, 2012 (Concluding that a governmental entity may not agree to defend a contractor against claims arising from acts or omissions of either the governmental entity or the contractor.)