RISK MANAGEMENT FOR LANDLORDS, TENANTS AND CONTRACTORS:

Through Contractual Provisions for Indemnity, Additional Insureds, Waiver of Subrogation, Limitation, Exculpation and Release

Volume 1: "*The Law*"

William H. Locke, Jr.
GRAVES, DOUGHERTY, HEARON & MOODY
515 Congress Avenue
Suite 2300
Austin, Texas 78701-3587
512-480-5736
blocke@gdhm.com

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TABLE OF CONTENTS

PAGE

RISK MANAGEMENT:

Through Contractual Provisions for Indemnity, Additional Insureds, Waiver of Subrogation, Limitation of Liability, Exculpation and Release

Risk shifting provisions are contained in all contracts. They are used in an attempt to assure the intended economic objectives of the "deal." The most common methods by which risk is shifted in a contract are by the use of representations and warranties, insurance covenants, express assumption of liabilities, indemnity, exculpation, release and limitation of liability provisions.

Every provision of a contract is either restating the rule that would be supplied by the court in the absence of the provision or is expressly shifting a risk from one party to the other.

This Article concerns provisions dealing with the shifting of "extraordinary" risk from one party to the other. Each contracting party's risk-related goals are (1) to accept no more risk than it can reasonably bear or insure, and (2) to transfer the balance of the risk to the other party. The following factors are involved in the ultimate determination as to how much risk a party receives or transfers: (1) which party is in the best position to control the extent of the occurrence of the risk?; (2) does one party have specialized knowledge of the type of risks most likely to occur and how to prevent or identify them?; (3) custom and practice in the particular industry (for example, sellers to buyers; landlords to tenants; owners to contractors; contractors to subcontractors); (4) the bargaining strength of the respective parties; and (5) statutory and common law public policies.

Indemnity agreements are common in most business relationships involving real estate. For example, the following types of agreements are indemnity agreements or are in the nature of indemnity agreements: title insurance, payment and performance bonds, and letters of credit. Indemnity agreements are contained in the following contracts: sales agreements, oil and gas leases, easements, agency agreements, construction contracts, loan agreements, notes (provisions for attorney's fees), and escrow agreements. Attached to this Article is an Appendix of Forms of extraordinary shifting of risks.

This Article is presented in two parts: **Volume 1** "***The Law***" and **Volume 2** "***The Forms.***" Volume 1 first addresses Texas law in the absence of an agreement. Additionally, the relationship of the statutorily-created doctrine of contribution to indemnity and the adoption of statutory schemes of allocating risk (comparative responsibility and the later adopted scheme of "proportionate responsibility") are explained. An approach to drafting a "successful" indemnity provision is explored. In the final part of Volume 1 the law as to exculpation, release, limitation of liability, insurance coverages, additional insured designations, and waiver of subrogation provisions as companions to indemnity provisions is analyzed. Volume 2 contains the most common forms used in commercial construction projects and office leases in Texas (*e.g.,* AIA A201 General Conditions and the State Bar of Texas *Real Estate Office Lease* form). Also included are alternative indemnity, insurance, and waiver provisions to effect a different shifting of risks than are contained in the "standard" forms. Accompanying each of these forms is a commentary noting the bias (the protected party) and a discussion of the risk allocations and the methods by which the risk is allocated. Also, included are the insurance endorsement forms commonly referenced in the construction contract and office lease risk management provisions and a commentary as to risk coverage and exclusions to coverage addressed by these insurance endorsements. Each of these forms has been annotated with footnotes identifying relevant case law and containing additional commentary explaining the risks being addressed by each form and certain gaps in coverage not addressed or possibly inadvertently being misaddressed. References in Volume 1 to forms in the Appendix refer to the form number of the form contained in Volume 2.

"*Indemnity*" is, "*I agree to be liable for your wrongs.*" Indemnity is a shifting of the risk of a loss from a liable person to another. However, many times scriveners use an indemnity provision when they do not know whether the indemnified person is a potentially liable person. Sometimes, an indemnity provision is no more than a restatement of existing duties, "*I will indemnify you for my wrongs*;" "*You will indemnify me for your wrongs.*"

An example of an **"*exculpation*"** provision is, "*I am not liable to you for my wrongs*." An exculpatory provision is designed to exclude, as between the parties to a contract, certain designated duties, liabilities or costs due to the occurrence or non-occurrence of events.

An example of a **"*release*"** is, "*You are not liable to me for your wrongs.*" A release is an agreement in which one party agrees to hold the other without responsibility for damage or other liability arising out of the transaction involved. *See Wallerstein v. Spirt*, 8 S.W.3d 774 (Tex.App.-Austin [3rd Dist.] 1999, *no writ*) - involving an indemnity by partners but not a release between partners.

The Texas Supreme Court has imposed certain requirements, such as the "fair notice" principle and the "express negligence" doctrine, in order for a liable party to be able to shift its liability for its negligence to another person. The concept of fair notice was introduced into Texas indemnity law by the Texas Supreme Court in *Spence & Howe Const. Co. v. Gulf Oil Corp.,* 365 S.W.2d 631, 634 (Tex. 1963). The fair notice principle focuses on the appearance and placement of the provision as opposed to its "content." The supreme court in *Spence* reasoned that

> [t]he obvious purpose of this rule is to prevent injustice. A contracting party should be upon *fair notice* that under his agreement and through no fault of his own, a large and ruinous award of damages may be assessed against him solely by reason of negligence attributable to the opposite contracting party.

Spence, at 634.

The Texas Supreme Court expressed frustration with the writing style and craft of Texas lawyers in *Ethyl Corp. v. Daniel Const. Co.*, 725 S.W.2d 705, 707 (Tex. 1987). In *Ethyl*, the court observed

> As we have moved closer to the express negligence doctrine, the scriveners of indemnity agreements have devised novel ways of writing provisions which fail to expressly state the true intent of those provisions. The intent of the scriveners is to indemnify the indemnitee for its negligence, yet be just ambiguous enough to conceal that true intent from the indemnitor. The result has been a plethora of lawsuits to construe those ambiguous contracts. We hold the better policy is to cut through the ambiguity of those provisions and adopt the express negligence doctrine.

The Texas Supreme Court in *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993) extended the fair notice principle and the express negligence doctrine to releases. Most recently, the Texas Supreme Court in *Houston Lighting & Power Co. v. Atchison, Topeka, & Santa Fe Railway Co.*, 890 S.W.2d 455 (Tex. 1994) expanded the express negligence doctrine to require indemnity agreements intending to cover an Indemnified Person's strict liability to expressly state that it covers such strict liability.

The most common method of risk management is through contractual provisions for insurance. The success of an entity's approach to contractual risk transfer can be considered successful if it meets the following criteria.

- Risks retained are appropriate and affordable.

- Risk as an element of the overall transaction and negotiation is incorporated at the onset.

- Indemnity, insurance, and other pertinent conditions are not so onerous that contact negotiations drag on unnecessarily delaying the transaction or necessitating the use of second-rate service providers to accomplish the contract's purpose.

- Contractual conditions allocating risk are not so onerous that a court disallows their operation at a future point in time.

- Insurance requirements are clear, using recognized terms that can be interpreted both at the time the contract is negotiated and in possible future disputes.

- Insurance and other support for the indemnity is in place when a loss occurs.

- A thorough insurance monitoring process keeps the transferee in compliance with the insurance requirements.

- The performance of the contract is monitored and regularly evaluated.

Criteria quoted from CONTRACTUAL RISK TRANSFER Strategies for Contract Indemnity and Insurance Provisions (International Risk Management Institute, Inc. 2003).

I. Indemnity Absent Contractual Indemnity Provisions.

A. Common Law: Basic Principles of Apportionment of Liability between Jointly Liable Persons.

1. Contribution and Indemnity Defined. The judicial rules and statutory schemes for "contribution" and "indemnity" establish the framework for apportioning liability between persons jointly and severally liable to third persons for negligence, strict liability and breach of warranty. For discussions of these rules and framework *see* 13 W. Dorsaneo, TEXAS LITIGATION GUIDE § 291.01 (1994) and Edgar and Sales, 4 TORTS AND REMEDIES, Chapter 102, Contribution and Indemnity (1991). *Also see* W. P. Keeton, PROSSER AND KEETON ON TORTS § 50 (5th Ed. 1985); Lee and Lindahl, MODERN TORT LAW (1989).

a. Joint and Several Liability. The common law of Texas recognized that persons who jointly contributed to cause injury, death or economic loss by their tortious conduct to a third person would be jointly and severally liable for their wrongdoing. This concept is aptly stated in *Landers v. East Texas Salt Water Disposal Co.*, 248 S.W.2d 731, 734 (Tex. 1952) as follows:

> Where the tortious acts of two or more wrongdoers join to produce an indivisible injury, that is, an injury which from its nature cannot be apportioned with reasonable certainty to the individual wrongdoers, all of the wrongdoers will be held jointly and severally liable for the entire damage and the injured party may proceed to judgment against any one separately or against all in one suit.

The joint tortfeasors, rather than the injured plaintiff, bear the burden of apportioning damages through the mechanisms of contribution and indemnity.

b. Indemnity. Indemnity is a mechanism by which all liability for a tort is shifted from one jointly liable defendant to another. *B&B Auto Supply, Sand Pit, and Trucking Co. v. Central Freight Lines, Inc.*, 603 S.W.2d 814, 816 (Tex. 1980); *see* Hodges, *Contribution and Indemnity Among Tortfeasors*, 26 TEX. L. REV. 150, 150-151 (1947).

c. Contribution. Contribution is a partial shifting from one jointly liable defendant to another defendant of a proportionate share of the damages. Contribution has been defined as "the payment by each tortfeasor of his proportionate share of the plaintiff's damages to any other tortfeasor who has paid more than his proportionate part." *See* Hodges, *supra*.

2. Common Law Exposure to Vicarious Liabilities. The common law imposed "vicarious" liability, sometimes called "imputed negligence", on persons in certain circumstances through the doctrine of *respondeat superior*, under which a master (employer) is liable for the torts of its servants. The *respondeat superior* doctrine imposes liability on the employer even though the employer did not contribute to the servant's negligent act. The independent contractor rule evolved as a means to combat the harshness of the general common law rule. Under the independent contractor exception a person is not liable for the negligence of its independent contractors. However, numerous exceptions evolved to the independent contractor exception resulting in the risk of the reimposition of liability even though the work is performed by independent contractors.

a. Employer-Employee v. Employer-Independent Contractor Relationships. As distinguished from the "employer-employee" relationship, the "employer-independent contractor" relationship exists in situations where the employer hires a third person to perform some act, but does not retain control of the means and methods used by the independent contractor to perform the act. Additionally, such independent contractors are generally specially skilled to perform the particular task. 44 TEX. JUR. 3d, *Independent Contractors* (1996).

b. Exceptions to the Independent Contractor Rule. Numerous exceptions evolved to the independent contractor rule to the point that the "exceptions swallowed the rule". W. P. Keeton, PROSSER AND KEETON ON THE LAW OF TORTS, § 71 (5th Ed. 1984).

(1) Liability to Third Parties for Acts of an Independent Contractor. As codified in the RESTATEMENT (SECOND) OF TORTS, §§ 410-429, a person is not liable for the acts or omissions of the independent contractor unless such person has been independently negligent. The following exceptions to this non-liability rule are recognized in Texas:

(a) Negligent Hiring. A person is liable for the negligent hiring of the contractor. 44 TEX. JUR. 3d, *independent contractors* § 56 *In general, selection of Incompetent Contractor* p. 283 (1996); *Simonton v. Perry,* 62 S.W. 1090 (Tex. Civ. App. 1901); *Webb v. Justice Life Ins. Co.*, 563 S.W.2d 347 (Tex. Civ. App.--Dallas, 1978, *no writ*).

(b) Work Unlawful or Creates Nuisance. Where the performance of the work contracted for is unlawful, or creates a nuisance, the employer may be responsible for injuries to third parties caused by the contractor. 44 TEX. JUR. 3d, *Independent Contractors,* § 56 *Unlawful Work* p. 291 (1996).

(c) Project Necessarily Causes Loss or Injury. The employer may not, to escape liability, contract for the project, the necessary or probable effect of which would be to injure others. 44 TEX. JUR. 3d, *Independent Contractors* § 68 *Project necessarily causes loss or injury* 293 (1996).

(d) Duties Imposed by Statute. If the prosecution of a project involves or results in a violation of a duty imposed by statute on the employer, the mere fact that the work was performed by a contractor will not relieve the employer from liability. 44 TEX. JUR. 3d, *Independent Contractors* (1996). So for instance the court held in *Sanchez v. MBank of El Paso*, 836 S.W.2d 151 (Tex. 1992) that the bank could not escape liability for the breach of the peace and wrongful repossession actions of its independent

contractor in repossessing plaintiff's bank financed automobile in violation of the requirements of TEX. BUS. & COMM. CODE § 9.503 (Vernon Supp. 2003).

(e) Exercise of Public Franchise. Where the work of a contractor involves the exercise of a franchise granted the employer, the latter must answer for the torts of the contractor and see to the proper execution of the granted power. 44 TEX. JUR. 3d, *Independent Contractors* § 72 *Exercise of public franchise* p. 296 (1996).

(f) Inherently Dangerous Work. A person employing an independent contractor to do an inherently dangerous work should see to it that the work is performed with such degree of care as is appropriate to the circumstances, or that all reasonable precautions be taken during its performance, so that third persons may be effectually protected against injury. The employer cannot delegate his duty of care to an independent contractor so as to relieve himself of his duty and the liability for the nonperformance of the duty. Thus, the employer may be held responsible to third persons for injuries that are the proximate results of the inherently dangerous nature of the work contracted for, whether the contractor's act was done negligently or otherwise. 44 TEX. JUR. 3d, *Independent Contractors* § 73 *Inherently dangerous work* p. 297 (1996).

(2) Liability for Injuries to Employees of an Independent Contractor. The most frequently encountered exceptions to the independent contractor rule are situations where the courts have imposed liability upon a person to the employees of an independent contractor. The following exceptions are recognized in Texas:

(a) Premises Liability--Safe Work Place. A person is liable if it "does not provide a safe work place". Actually, this statement of the rule is too broad. More accurately phrased, the rule requires the owner or occupier to exercise ordinary car to keep the premises in reasonably safe condition so that the employee of the independent contractor will not be injured. *Redinger v. Living, Inc.*, 689 S.W.2d 415 (Tex. 1985); 59 TEX. JUR. 3d *Premises Liability § 25 Duty owed business invitee 168 and § 43 Failure to provide safe place to work p. 270* (1996).

See, for instance, *Stablein v. Dow Chemical Co.,* 885 S.W.2d 502 (Tex. App.--El Paso 1994, *no writ*) where the court found that the premises owner was not liable for injuries to an employee of a subcontractor (cafeteria worker employed by a cafeteria services contractor working at the Dow plant). The condition encountered by the employee (a crate in the food freezer) was not a dangerous condition peculiar to the work being performed by the contractor. The contract with the contractor recognized that Dow did not retain control over the method of the contractor performing its work. The injury arose out of an activity conducted by the employee in the course and scope of the employees employment by the contractor. Dow's duty to the employee was that owed by an occupier of land to a business invitee--to warn the contractor and its employees of any hidden dangers existing on the premises.

The court of appeals in *Schley v. Structural Metals, Inc.*, 595 S.W.2d 572 (Tex. Civ. App.--Waco 1979, *writ ref'd n.r.e.*) held that the abolition of the "no duty" rule in occupier-invitee cases, in light of the adoption of the Comparative Negligence and Contribution Statute in 1973 (discussed *infra*), necessarily set aside the rule that the knowledge of the independent contractor relieved the owner or occupier of land of any duty to protect or warn the employees of the independent contractor of dangers on the premises (even "open and obvious dangers").

An employer may be liable for injuries suffered by the employee of an independent contractor as a result of a defective appliance furnished by him. 44 TEX. JUR.3d, *Independent Contractors,* § 48 *Furnishing dangerous appliances* p. 275 (1996).

Similarly, a contractor in control of the premises owes a duty to the employees of its subcontractor similar to the duty owed by the owner to the contractor as to the premises. 44 TEX. JUR.3d, *Independent Contractors,* § 49 *General contractors* 276 (1996).

Liability is imposed upon the employer of the contractor in cases where the independent contractor's work involves a dangerous condition on the owner's premises which causes injury to the contractor's employees. The exception is summarized in the RESTATEMENT (SECOND) OF TORTS (1966) as follows:

> **413. Duty to Provide for Taking of Precautions Against Dangers Involved in Work Entrusted to Contractor**. One who employs an independent contractor to do work which the employer should recognize as likely to create, during its progress, a peculiar risk of physical harm to others unless special precautions are taken, is subject to liability for physical harm caused to them by the absence of such precautions if the employer:
>
> (a) fails to provide in the contract that the contractor shall take such precautions, or
>
> (b) fails to exercise reasonable care to provide some other manner for the taking of such precautions.
>
> **416. Work Dangerous in Absence of Special Precautions**. One who employs an independent contractor to do work which the employer should recognize is likely to create during its progress a peculiar risk of physical harm to others unless special precautions are taken, is subject to liability for physical harm caused to them by the failure of the contractor to exercise reasonable care to take such precautions, even though the employer has provided for such precautions in the contract or otherwise.
>
> **4.22. Work on Buildings and Other Structures on Land**. A possessor of land who entrusts to an independent contractor construction, repair, or other work on the land, or on a building or other structure upon it, is subject to the same liability as though he had retained the work in his own hands to others on

> or outside of the land for physical harm caused to them by the unsafe condition of the structure:
>
> (a) While the possessor has retained possession of the land during the progress of the work, or
>
> (b) After he has resumed possession of the land upon its completion.
>
> **427. Negligence as to Danger Inherent in the Work**. One who employs an independent contractor to do the work involving a special danger to others which he contemplates or has reason to contemplate when making the contract, is subject to liability for physical harm caused to such others by the contractor's failure to take reasonable precautions against such danger.

The introductory comments to these rules offers the following rationale:

> The rules stated in the following §§ 416-429, unlike those stated in the preceding §§ 410-415, do not rest upon any personal negligence of the employer. They are rules of **vicarious liability**, making the employer liable for the negligence of the independent contractor, irrespective of whether the employer has himself been at fault. They arise in situations in which, for reasons of policy, the employer is not permitted to shift the responsibility for the proper conduct of the work to the contractor. The liability imposed is closely analogous to that of a master for the negligence of a servant.

(b) Retention of Control by Employer. Liability is imposed on the employer of the contractor where the employer retains control of the manner and means of the independent contractor's performance of its work.

Section 414 of the RESTATEMENT (SECOND) OF TORTS (1966) states the common law rule as follows:

> **414. Negligence in Exercising Control Retained by Employer**. One who entrusts work to an independent contractor, but who retains the control of any part of the work, is subject to liability for physical harm to others for whose safety the employer owes a duty to exercise reasonable care, which is caused by his failure to exercise control with reasonable care.

Comment c. to § 414 notes that in order to succeed in a cause of action against an employer, the plaintiff must prove: (1) the owner- occupier retained control and supervision of the details of the work to the extent that the independent contractor was no longer free to do the job its own way, and (2) such retained control contributed to the incident.

Similarly, Comment c. states the following as to the liability of a contractor for injuries to employees of its subcontractor:

> It is not enough that (the employer) has merely a general right to order the work stopped or resumed, to inspect its progress or receive reports, to make suggestions or recommendations which need not necessarily be followed, to prescribe alterations or deviations. Such a general right is usually reserved to employers, but it does not mean that the contractor is controlled as to his methods of work, or as to his operative detail. There must be such retention of a right of supervision that the contractor was not free to work his own way.

(c) Borrowed Servant Doctrine. Another exception is the "borrowed servant" doctrine. Under the borrowed servant doctrine the employer of the independent contractor becomes the employer of the independent contractor's employees. Sometimes the employer is called the "special employer" under these circumstances. The following factors have been used by the courts to find a "borrowed servant" relationship: (1) the right of the special employer to control the details of the employee's performance *USF & G v. Goodson,* 568 S.W.2d 443 (Tex. Civ. App.-- Texarkana 1978, *writ ref'd n.r.e.*), but a contractual retention of control is not necessary, if actual control is exercised *Exxon Corp. v. Perez,* 842 S.W.2d 629 (Tex. 1992); (2) if the "special employer" pays the amount of the premiums for workers compensation insurance to the employer *Marshal v. Toys-R-Us Ntyex, Inc.,* 825 S.W.2d 193 (Tex. App.–Houston [4th Dist.] 1992, *writ denied*); (3) the right to hire and discharge, the obligation to pay wages, the carrying of the worker on the social security and income tax withholding rolls of the special employer; and (4) the furnishing of tools to the employee.

3. Why Contractual Indemnification? Contractual indemnity provisions are a means of shifting the burden of loss from one potentially liable person to another person. Contractual indemnity is used to alter the apportionment of liability provided by judicial rules and statutory schemes for "contribution" and "indemnity." Through the use of contractual indemnity agreements, the parties are shifting the risk of extraordinary liability arising out of a breach of a common law duty imposed upon the parties; the duty itself is not shifted. The following are examples of when the law allocates liability absent contractual indemnity:

a. Abolition of Common Law Indemnity Except in Limited Circumstances. Prior to the abolition of common law indemnity, a joint tortfeasor could obtain indemnity from another joint tortfeasor where the joint tortfeasors were not in *pari delicto* as to each other, as where the injury resulted from a violation of a duty one owed the other. The legislative Comparative Apportionment Schemes relieved the rigor of the common law bar against contribution in cases involving joint tortfeasors who were determined to be in *pari delicto*.

(1) Areas in Which Common Law Indemnity is Still Available. The adoption of the various legislative liability apportionment schemes resulted in the courts' abandonment of the doctrine of common law indemnity except in the following narrow situations: (a) cases where the joint tortfeasor's liability is purely vicarious, for example a principal liable for an agent's wrongdoing under the doctrine of *respondeat* superior, or (b) cases where a retailer is merely an innocent conduit in the sale of a defective product. In

each of these situations, the common law doctrine of indemnity is still available in Texas as between the joint tortfeasors to shift full liability from the "innocent" party to the "wrongdoer."

The effect of the adoption of the various comparative legislative apportionment schemes, and the holdings in *B&B Auto Supply* and *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984) and their progeny, is to limit common law indemnity to the following narrow circumstances.

In 1980 the Texas Supreme Court in *B&B Auto Supply* stated

> We ... hold that the common law right to indemnity is no longer available between joint tortfeasors in negligence cases ... . Our holding is not intended to bar indemnity in cases in which one party's liability is purely vicarious. We express no opinion whether this holding would extend to a strict liability case or a case involving a combination of negligent and strictly liable tortfeasors.

B&B Auto Supply, Sand Pit, and Trucking Co. v. Central Freight Lines, Inc., 603 S.W.2d 814, 817 (Tex. 1980).

The Texas Supreme Court in *Bonniwell v. Beech Aircraft Corp.*, 663 S.W.2d 816 (Tex. 1984) summarized the impact of *B&B Auto Supply* and *Duncan v. Cessna Aircraft* on common law indemnity as follows:

> ... Article 2212a has abolished the common law doctrine of indemnity between negligent joint tortfeasors (citations omitted). In *Duncan*, we likewise impliedly abolished the common law doctrine of indemnity between joint tortfeasors in strict liability cases.
>
> Only a vestige of common law indemnity remains. In *B&B Auto Supply*, we recognized the survival of common law indemnity with respect to liability of a purely vicarious nature. An analogous indemnity right survives in products liability cases to protect the innocent retailer in the chain of distribution. This is all that remains of the common law doctrine of indemnity. (Court's emphasis.)

Bonniwell v. Beech Aircraft Corp., 663 S.W.2d 816, 819 (Tex. 1984).

(a) Purely Vicarious Liability. Common law indemnity is still available where a joint tortfeasor's liability is purely vicarious, as in the case of respondent superior. *Bonniwell v. Beech Aircraft Corp.*, 663 S.W.2d 816, 819-20 (Tex. 1984); *Knutson v. Morton Foods, Inc.*, 603 S.W.2d 805, 808 (Tex. 1980); *Cypress Creek Utility Service Co., Inc. v. Muller*, 640 S.W.2d 860, 864 (Tex. 1982). An agent who does not follow his agency contract has been held liable to indemnify his principal from liabilities so resulting. *Hartford Casualty Ins. Co. v. Walker County Agency, Inc.*, 808 S.W.2d 681, 687-88 (Tex. App.--Corpus Christi 1991, *no writ*).

(b) Innocent Retailer. A retailer who does nothing except to serve as an innocent conduit in the sale of a product is entitled to indemnity from those upstream in the distribution chain. *Duncan* at 432; *Bonniwell* at 819-820; *General Motors Corp. v. Simmons*, 558 S.W.2d 855, 860-61 (Tex. 1977); *Jackson v. Freightliner Corp.*, 938 F.2d 40, 42 (5th Cir. 1991)--trailer manufacturer failed to prove it was a purely innocent conduit of a defectively-manufactured trailer. This vestige of common law indemnity includes indemnity by the product manufacturer for the innocent retailer's successful defense of a product's liability claim. The court in *Central Consolidated, Inc. v. Robertshaw Controls Co.,* 868 S.W.2d 910 (Tex. App.--Beaumont 1994, *no writ*) found that the trial court erred in granting a summary judgment against the retailer on its claim against the manufacturer for the retailer's attorney's fees after the jury found the retailer to be innocent of wrongdoing. The court held that the retailer could continue the litigation for the sole purpose of determining whether the manufacturer had manufactured a defective product and, as a result, had to indemnify the retailer for its attorney's fees incurred in defending the products liability action.

(c) Fraud. The court of appeals, in *Smith v. Herco, Inc.*, 900 S.W.2d 852, 863 (Tex. App.--Corpus Christi 1995, *writ denied*), permitted a joint tortfeasor to recover by common law indemnity from the other defendant joint tortfeasor based on a jury's finding that the second tortfeasor was guilty of fraud which caused the common liability.

(2) Strict Construction of Availability of Common Law Indemnity. The narrowness with which the courts construe the availability of common law indemnity is exemplified by the recent case of *LTV Energy Products Co. v. Chaparral Inspection Co.*, 827 S.W.2d 593 (Tex. App.--Houston [1st Dist.] 1992, *writ denied*). In *Chaparral*, LTV sought to recover indemnity from Chaparral for $828,472 paid by LTV to settle a claim brought against it in a Mississippi lawsuit. LTV along with Joe Bonner, Inc. was sued by Hughes Eastern when pipe inspected by Chaparral for Bonner, and sold by Bonner to LTV then resold by LTV to Hughes Eastern failed. After Bonner and LTV settled the claims against them in the Mississippi suit, LTV sued Chaparral. The court held that LTV's indemnity claim did not fall within the remaining common law rights to indemnity. The court held

> The case before us does not fall within any of the three exceptions. LTV and Chaparral had no contract providing for indemnification. Chaparral, as an inspector of the well casing for LTV's upstream supplier, was not a member of the marketing chain. Finally, there is no agency or surety relationship between LTV and Chaparral that would allow LTV to assert a vicarious liability theory.
>
> In *American Alloy Steel v. Armco, Inc.*, 777 S.W.2d 173 (Tex. App.--Houston [14th Dist.] 1989, *no writ*), the court was faced with a quite similar situation. American Alloy had a contract to buy steel plating from Armco. When American Alloy's subsequent buyer alleged that the plating was defective, American Alloy replaced it and sued Armco for reimbursement under an indemnity theory. ... In reaching its decision, the Fourteenth Court of Appeals stated: "There is no contractual

provision for indemnity in the case before us. Therefore, we must determine whether the relationship between American Alloy and Armco is such that either in law or in equity, we may imply a right to indemnity on American Alloy's behalf. More specifically, does an implied obligation of indemnity arise out of the contractual relationship between the two companies?"

> In the case at bar, LTV and Chaparral have a far more tenuous relationship than the parties in *American Alloy*, where the mere fact of a contractual business relationship between the parties was not held to give rise to an implied obligation of indemnity. We conclude from *American Alloy* that a situation in which two parties have no contractual business dealings--in fact, no direct business dealings whatsoever--is an improper place to imply an obligation of indemnity.

See infra **IA3a(1)** Indemnity Absent Contractual Indemnity Provisions - Common Law: Basic Principles of Apportionment of Liability Between Jointly Liable Person - Why Contractual Indemnification - Abolition of Common Law Indemnity Except in Limited Circumstances - **Areas in Which Common Law Indemnity is Still Available** for a further discussion of the vestiges of common law indemnity.

(3) Unavailability of Attorney's Fees in Enforcing Common Law Indemnity. Absent some statutory grounds for obtaining attorney's fees in enforcing a common law indemnity, Texas courts will not award reimbursement to the common law indemnitee for its attorney's fees in suing the common law indemnitor to collect on the indemnity. Although attorney's fees incurred in the defense of a plaintiff's liability claim are considered "damages" to which common law indemnity can apply, attorney's fees incurred to collect on the indemnity are not indemnified. This point can be covered in an indemnity contract. Also, attorney's fees incurred in the settlement of a claim can be included in the Indemnified Liabilities covered by a contractual indemnity which otherwise are not embraced in common law indemnity.

b. Abolition of Common Law Defenses and Adoption of Statutory Comparative Apportionment Schemes. With the advent of the statutorily-enacted comparative negligence and Comparative Responsibility and Apportionment Schemes of apportioning liability among joint tortfeasors, the courts have eliminated many of the previously available common law defenses that lessened the opportunity for plaintiffs to recover: doctrine of "no duty" abolished - *Parker v. Highland Park, Inc.*, 565 S.W.2d 512, 517 (Tex. 1978); doctrine of "imminent peril" abolished - *Davila v. Sanders*, 557 S.W.2d 770, 771 (Tex. 1977); doctrine of "assumption of risk" abolished - *Farley v. MM Cattle Co.*, 529 S.W.2d 751, 758 (Tex. 1975); and the doctrine of "contributory negligence" (however slight) barred recovery replaced with "**51% Bar Rule**" - TEX. CIV. PRAC. & REM. CODE ANN. § 33.001 (Vernon 1997). The comparative negligence, comparative responsibility and proportionate responsibility statutes have given joint tortfeasors, which are jointly and severally liable, contribution rights to recover, as between themselves, payments made in excess of their assigned percentage of liability.

However, the adoption of these legislative systems, the advent of products liability, and the abolition of common law indemnity, also highlight the need to consider contractual indemnity to shift complete liability between joint tortfeasors or even from one tortfeasor to another tortfeasor not held responsible at law.

c. Cases Prohibiting Contribution or Indemnity from a Responsible Person. In the situations outlined below, statutes or case law may create bars to contribution. The existence of these bars to recovery can be addressed by contractual indemnity.

(1) Parental Immunity. The Texas Supreme Court in *Shoemake v. Fogel, Ltd.*, 826 S.W.2d 933 (Tex. 1992) held that a deceased child's estate's recovery for wrongful death could not be reduced by the percentage of contributory negligence of the mother. The child died four months later as a result of a near-drowning in an apartment project swimming pool. The jury allocated negligence 55% to the apartment owner and management company and 45% to the mother for negligent supervision. The supreme court upheld the reduction of the damages on the wrongful death claim of the mother by her 45% comparative negligence, but held that the parent's comparative negligence could not be used to reduce the child's estate's recovery under the survival statute. The doctrine of parental immunity prevented a comparative negligence claim being imputed against the child's right of recovery on the survival claim. *See* TEX. CIV. PRAC. & REM. CODE ANN. §§ 71.001-.011 (Vernon 1997) (wrongful death), § 71.021 (Vernon 1997) (survival). The supreme court had previously adopted restrictions on the parental immunity doctrine in *Felderhoff v. Felderhoff*, 473 S.W.2d 928 (Tex. 1971)- suits arising in the course of the parent's business activities, and *Jilani v. Jilani*, 767 S.W.2d 671 (Tex. 1988)-automobile tort action, but reaffirmed its view that a parent retains immunity as to "alleged acts of ordinary negligence which involve a reasonable exercise of parental discretion with respect to provisions for the care and necessities of the child." *Felderhoff* at 933; *Jilani* at 672.

The supreme court also cited for its holding the following rule in *Varela v. American Petrofina Co. of Texas, Inc.*, 658 S.W.2d 561, 562 (Tex. 1983)--a defendant's claim of contribution is derivative of the plaintiff's right to recover from the joint defendant against whom contribution is sought: "Thus, [the complex's] claim of contribution depends upon whether [the girl's] estate has the right to recover damages from [the mother]." The court concluded that because the girl's estate had no viable negligence claim against the mother, the complex has no viable contribution claim against the mother.

The apartment lease apparently did not contain a contractual indemnity provision whereby the mother agreed to indemnify the apartment owner against (a) all liabilities (100% of damages on the wrongful death claim and the survival claim) arising out of the concurrent negligence of the mother and the complex, and/or (b) all damages arising out of a survival action of the child's estate, and/or (c) an apportionment of damages (45%) on the survival claim due to the comparative negligence of the mother.

(2) Workers' Compensation Bar to Contribution. In *Varela v. American Petrofina Co. of Texas, Inc.*, 658 S.W.2d 561 (Tex. 1983) the Texas Supreme Court held that an employer's negligence could not be considered in a third-party negligence action bought by an employee arising out of an accidental injury covered by workers' compensation insurance. The jury had determined that the accident was attributable as follows: plant owner's negligence (Petrofina)-43%, employer's negligence (Hydrocarbon Construction)-42%, and employee's negligence (Varela)-15%. The supreme court reversed the trial court's reduction of the damage award from $606,800 to $243,924, or 43% of total damages. The supreme court held that the Workers' Compensation Act is an exception to the Comparative Negligence Statute [then Article 2212a, § 2(b)] and disallowed contribution from the employer. The court concluded:

> We hold that Article 8306, § 3 (the Texas Workers' Compensation Act) is an exception to Article 2212a, § 2(b) (the Comparative Negligence Statute). When read together those two Articles indicate the intent of the Legislature that where the third party defendant's negligence is greater than that of the employee, the employee shall recover the total amount of damages as found by the jury diminished only in proportion to the amount of the negligence attributed to the employee.
> ...
> Further, a defendant's claim of contribution is derivative of the plaintiff's right to recover from the joint defendant against whom contribution is sought. (citing authorities) The Workers' Compensation Act, Article 8306, § 3, precludes any right by Varela to a cause of action against Hydrocarbon for common law negligence. (omitted authority) Since Varela had no cause of action against Hydrocarbon, Petrofina had no claim for contribution from Hydrocarbon. Since Petrofina had no claim for contribution, § 2(e) of Art. 2212a has no application to this case.

Id. at 562-63.

The enforceability of a contractual indemnity passing back to the employer a third-party's negligence over the "Workers' Compensation Bar" has been upheld. *Enserch Corp. v. Parker*, 794 S.W.2d 2, 7 (Tex. 1990). The Texas Workers' Compensation Act provides that a subscribing employer has no liability to reimburse or hold another person harmless for a judgment or settlement resulting from injury or death of an employee "unless the employer executed, before the injury or death occurred, a written agreement with the third party to assume the liability." Texas Workers' Compensation Act, TEX. LABOR CODE § 417.004 (Vernon 1996), repealing TEX. REV. CIV. STAT. ANN. Art. 8308-4.04 (Vernon 1996), formerly Art. 8306, § 3(d) (Vernon 1986). § 417.004 of the Texas Labor Code provides as follows:

> In an action for damages brought by an injured employee, a legal beneficiary, or an insurance carrier against a third party liable to pay damages for the injury or death under this Chapter that results in a judgment against the third party or a settlement by the third party, the employer is not liable to the third party for reimbursement or damages based on the judgment or settlement *unless the employer executed, before the injury or death occurred, a written agreement with a third party to assume the liability*. (Emphasis added.)

Suits brought by the indemnitee (the Indemnified Person) under an indemnity agreement against the indemnitor (the Indemnifying Person) in the context of an employer having indemnified a third party for injuries occurring to the employer's employees due in part to the negligence of the employer are commonly referred to as "third-party- over actions". The "written agreement" requirement in the Workers' Compensation Act for overcoming the "Workers' Compensation Bar" prevents oral indemnity agreements from being enforced against an employer for employee injuries.

However, as noted *infra* in the discussion of the Texas Supreme Court's holding in *Ethyl Corp. v. Daniel Const. Co*., care has to be used in drafting a contractual indemnity to overcome both the "express negligence" test of the Texas Supreme Court and the Workers' Compensation Bar. The court in *Ethyl* held that the contractual indemnity in the contract between Ethyl (the property owner) and Daniel (the contractor/employer) requiring Daniel to indemnify Ethyl for all injuries to persons "caused by the negligence or carelessness of Contractor" was not adequate either to indemnify Ethyl against an injury to Daniel's employee caused by the concurring negligence of Ethyl (90%) and Daniel (10%) or even against the portion of the negligence attributable to Daniel.

The indemnity provision did not expressly state that it covered injuries occurring as a result of the negligence of the indemnified person (Ethyl) and as to the portion attributable to Daniel, it did not expressly state that it covered cases where Daniel was concurrently negligent. "Ethyl next contends it is entitled to comparative indemnity to the extent of Daniel's negligence which the jury found to be 10%. However, the contract in question contains no provision for contractual comparative indemnity." *Ethyl* at 708. *Also see B-F-W Const. Co., Inc. v. Garza*, 748 S.W.2d 611 (Tex. App.--Ft. Worth 1988, *no writ*).

4. Historical Relationship of Contribution and Indemnity.

a. Doctrine of in *Pari Delicto*. Early English and American courts refused to adjust the financial burdens between defendants who were regarded by the court as being equally blameworthy. Therefore, joint tortfeasors who were "in *pari delicto*" had no rights to contribution at common law. However, the courts held that they had power in equity to aid a tortfeasor who was relatively blameless by granting indemnity. *See* W. P. Keeton, PROSSER AND KEETON ON TORTS (5th ed. 1985).

b. Prior to 1980, Indemnity was Granted in Texas if the Tortfeasors were not in *Pari Delicto*. Prior to 1980, Texas courts viewed the availability of indemnity between jointly liable defendants based on whether: (1) the court viewed the defendants as being equally at fault relative to the plaintiff (in *pari delicto*) or (2) the defendants were not equally at fault (not in *pari delicto*) with indemnity being allowed ("an all or

nothing approach to indemnification"). *See* Phifer, *Contribution and Indemnity*, HANDLING INSURANCE AND TORT CLAIMS SEMINAR (UNIV. HOU. 1991).

The courts envisioned two torts: one tort committed by the defendants against the plaintiff, the second committed by one of the defendants against the other, which gave rise to indemnity.

For example, indemnity was held to be available in cases where an employer was held to be liable along with its employee for the employee's negligently inflicting an injury on a third person. In such cases, the courts held that the employer and the employee were not in *pari delicto*, in other words not equally at fault. The employer who paid the plaintiff's damages was entitled to indemnity from the employee. This principle was stated by the Texas Supreme Court in *Austin Road Co. v. Pope*, 216 S.W.2d 563, 565 (Tex. 1949) as follows:

> Thus, where the parties are not equally guilty, the principal delinquent may be held responsible to a codelinquent for damages paid by reason of the offense in which both participated in different degrees as perpetrators ... . In order to determine whether the loss should be shifted from one tortfeasor to another the proper approach is to consider the one seeking indemnity as though he were a plaintiff suing the other in tort, and then determine whether such a one as plaintiff, though guilty of a wrong against a third person, is nevertheless entitled to recover against his co-tortfeasor. Texas L. Rev., Vol. XXVI, p. 150.

c. 1980 Abolition of Common Law Indemnity Except In Narrow Exceptions. After 1980, in the absence of a well-drafted contractual indemnity provision, common law indemnity for tort damages is not available in Texas except under narrow exceptions.

(1) Legislative Enactment of Contribution and Comparative Negligence Statutes. Prior to the enactment in 1987 of the current scheme of Comparative Responsibility and Apportionment, the legislature had enacted statutes in 1917 and 1973 establishing rights of contribution between certain jointly liable tortfeasors. Texas courts developed an elaborate body of indemnity law and coordinated it with the 1917 and 1973 Statutes.

(a) 1917 Statute. In 1917, the legislature enacted a mechanism for jointly and severally liable defendants to obtain contribution from other jointly and severally liable defendants. *See* §§ 32.001-32.003 of the Civil Practice and Remedies Code, formerly TEX. REV. CIV. STAT. ANN. Art. 2212 (referred to herein as the **"1917 Statute"**).

i) Contribution Scheme: Equal Apportionment Rule. The 1917 Statute provides that a jointly liable tortfeasor may recover from the other liable tortfeasors "an amount determined by dividing the number of all liable defendants into the total amount of the judgment." TEX. CIV. PRAC. & REM. CODE ANN. § 32.003(a). (Vernon 1997)

ii) Superseding Legislative Contribution Systems. Although the 1917 Statute applied to all tort actions, a separate scheme for negligence actions was set up in 1973. Further in 1987, an elaborate amendment set up a statutory scheme of "Comparative Responsibility" for products liability, professional liability cases, negligence and mixed theory cases. The legislature subsequently enacted a "Proportionate Responsibility" scheme as a part of the 1995 tort reforms. Amendments to § 33.001 and their effective date are discussed below (the **"1995 Proportionate Responsibility Statute"**).

iii) Prerequisites for Contribution. There are four prerequisites for recovery of contribution under the 1917 Statute:

a) Judgment Against Defendant. The first prerequisite is that a court must have rendered a judgment against the defendant seeking contribution. TEX. CIV. PRAC. & REM. CODE ANN. § 32.002 (Vernon 1997).

b) Payment of Judgment. The defendant seeking contribution must have paid the judgment so as to discharge all joint tortfeasors' liability to the plaintiff, or at least a "disproportionate share" of the common liability. TEX. CIV. PRAC. & REM. CODE ANN. § 32.002 (Vernon 1997).

c) Joint Tortfeasor. The one from whom contribution is sought must be a joint tortfeasor with the defendant seeking contribution. TEX. CIV. PRAC. & REM. CODE ANN. § 32.002 (Vernon 1997).

d) No Other Applicable Contribution Scheme. There must be no other statutory or common law rights of contribution, indemnity, or other recovery between the defendant seeking contribution and the ones from whom contribution is sought. TEX. CIV. PRAC. & REM. CODE ANN. § 32.001(b) (Vernon 1997).

(b) 1973 Statute. In 1973, the legislature adopted a Comparative Negligence and Contribution Statute applicable to apportionment of contribution between tortfeasors whose joint and several liability is grounded in negligence alone. *See* former TEX. CIV. PRAC. & REM. CODE ANN. § 33.001, *et seq.* (Vernon 1997) which was originally enacted as TEX. REV. CIV. STAT. ANN. Art. 2212a (Vernon 1973) (herein referred to as the **"1973 Statute"**).

i) Application to Contribution for Cases Involving Only Negligence between 1973 and 1987. The Comparative Negligence and Contribution scheme was superseded by the 1987 Statute. Therefore, the 1973 Statute applies to cases arising after September 1, 1973, and for which suit is filed before September 1, 1987, whose joint and several liability is grounded in negligence alone. *See General Motors Corp. v. Simmons*, 558 S.W.2d 855, 861-62 (Tex. 1977) in which the Texas Supreme Court concluded that the 1973 Statute did **not apply to a mixed theory** of recovery case where a manufacturer was held liable both for negligence and in strict liability and the employer of the driver of the car was held to be

liable in negligence. In *Simmons*, the Texas Supreme Court held that this type of mixed theory case was governed by the Equal Apportionment Rule under the 1917 Statute. This position was subsequently overturned in *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984) and after that by the 1987 Statute.

ii) Contribution Scheme: Percentage Comparison and Allocation System. The 1973 Statute substituted a percentage comparison and allocation system for the equal sharing scheme of the 1917 Statute and modified the joint and several liability rule.

a) Abolition of Contributory Negligence Bar. The 1973 Statute replaced the common law rule that any contributory negligence (however slight) of the plaintiff completely barred plaintiff's recovery with a system of "modified" comparative negligence. Under the Modified Comparative Negligence system, the jury is required to assign to the plaintiff and to each defendant a percentage of the total negligence that proximately caused the plaintiff's injuries. If the plaintiff is found to have contributory negligence equal to or less than the combined negligence of the defendants, then the plaintiff's damages are proportionately reduced, but recovery is not barred. Art. 2212a, § 1 (Vernon 1973), codified as former TEX. CIV. PRAC. & REM. CODE ANN. § 33.001(b) (Vernon 1986).

b) Defendant More Negligent than Plaintiff. Each defendant whose negligence equals or exceeds the plaintiff's contributory negligence is jointly and severally liable for the entire amount of the plaintiff's judgment, but has rights of contribution for amounts in excess of such defendant's proportionate share. Contribution was in proportion to the percentage of negligence attributable to each defendant. Art. 2212a, § 2(b) and (c) (Vernon 1973), as codified as former TEX. CIV. PRAC. & REM. CODE ANN. §§ 33.012, 33.013 (Vernon 1986).

c) Defendant Less Negligent than Plaintiff. In cases where the combined negligence of the defendants was equal to or greater than the contributory negligence of the plaintiff, each defendant whose negligence was less than the plaintiff's contributory negligence was liable only for that portion of the judgment that represents such defendant's percentage of negligence. Art. 2212a § 2(c) (Vernon 1973), codified as former TEX. CIV. PRAC. & REM. CODE ANN. § 33.013 (Vernon 1986). If the plaintiff was more negligent than the defendant, then the plaintiff's contributory negligence would still bar recovery against the defendant. *Murff v. U.S.*, 785 F.2d 552 (5th Cir. Tex. 1986), *cert. denied*, 479 U.S. 823 (1986); *Jannette v. Deprez*, 701 S.W.2d 56 (Tex. App.--Houston [5th Dist.] 1985, *writ ref'd n.r.e.*).

Example: Assume that A, B, and C negligently injure Plaintiff.

> In a suit filed before September 1, 1987, the jury finds that Plaintiff's damages total $100,000 and that the percentages of negligence are as follows: Plaintiff-- 15%, A--45%, B--30%, C--10%. The 1973 Statute produces the following results:
>
> (1) Plaintiff may recover $85,000 because his contributory negligence reduces the $100,000 by 15%.
>
> (2) A and B are jointly and severally liable for the entire $85,000 because their percentages of negligence, 45% and 30% respectively, are higher than Plaintiff's 15% contributory negligence.
>
> (3) C is liable to Plaintiff for only $10,000 because his 10% of negligence is less than Plaintiff's 15% of contributory negligence.
>
> (4) A has rights of contribution from B not to exceed $30,000 and from C not to exceed $10,000. Therefore, A's ultimate liability for damages is $45,000.
>
> (5) B has rights of contribution from A not to exceed $45,000 and from C not to exceed $10,000. Therefore, B's ultimate liability for damages is $30,000.

Since the 1973 Statute does not address the insolvency of a liable defendant, in the above example A bears the burden of B's insolvency, but C bears none of the burden of B's insolvency.

The above example is contained in Edgar and Sales, 4 TORTS AND REMEDIES, Ch. 102, *Contribution and Indemnity* 38 (1991).

(2) Adoption of the Statutory Comparative Negligence and Contribution System as Abolishing Common Law Indemnity.

(a) 1980: *B&B Auto Supply*. The Texas Supreme Court in *B&B Auto Supply, Sand Pit, and Trucking Co. v. Central Freight Lines, Inc.*, 603 S.W.2d 814 (Tex. 1980) held that there could not be common law indemnity due to the adoption of the Comparative Negligence and Contribution Statute in 1973. The *B&B Auto Supply* case involved two defendants who were held jointly liable for the plaintiff's injuries and the jury apportioned negligence between the defendants as being 1/3 to B&B and 2/3 to Central Freight. The court reasoned that the common law doctrine of indemnity, totally shifting liability from one tortfeasor to another, was inconsistent with the 1973 Comparative Negligence and Contribution Statute that required the trier of fact to attribute a percentage of negligence to each tortfeasor. The supreme court pointed out that the 1973 Contributory Negligence and Contribution Statute displaced the "all or nothing" defenses of contributory negligence, no duty, imminent peril, and assumption of the risk. The supreme court held:

> Since the enactment of Art. 2212a we have sought to abolish doctrines directed to the old choice of total victory and total defeat. [Citations omitted.] The policy underlying these decisions and the enactment of Art. 2212a was to abolish traditional common law rules which required an all or nothing result and to return trials of negligence cases to tort concepts of negligence and comparative negligence. The common law doctrine of indemnity is yet another of these common law rules which results in shifting total responsibility for a tort from one party

to another. Under Art. 2212a, there is no longer any basis for requiring one tortfeasor to indemnify another tortfeasor when both have been found negligent and assessed a percentage of fault by the jury.

Id. at 817.

(b) Subsequent Cases. *Also see* the following subsequent Texas Supreme Court decisions reaffirming the holding that the Comparative Negligence and Contribution Statute abolished common law indemnity even though abolition of the doctrine is not mentioned in the statute: *Aviation Office of America, Inc. v. Alexander & Alexander of Texas, Inc.*, 751 S.W.2d 179, 180 (Tex. 1988) (*per curiam*); *Bonniwell v. Beech Aircraft Corp*., 663 S.W.2d 816, 819 (Tex. 1984); *Cypress Creek Utility Service Co., Inc. v. Muller*, 640 S.W.2d 860, 863 (Tex. 1982).

d. 1984 Judicial Adoption of Comparative Causation and Apportionment Scheme.

(1) Setting for Judicial Intervention. Prior to *Duncan*, there were three separate theories for recovery in products liability cases and each had a different means of handling contribution between jointly liable defendants. *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984).

(a) Multiple Products Liability Recovery Theories. A plaintiff could recover on a products liability suit on tort theories of negligence and strict liability and on the contract theory of breach of warranty. In 1967 the Texas Supreme Court had adopted Section 402A of the RESTATEMENT (SECOND) OF THE LAW OF TORTS (1966) as the basis for the strict liability cause of action. *McKisson v. Sales Affiliates, Inc*., 416 S.W.2d 779, 783-784 (Tex. 1967).

(b) Different Apportionment Schemes Applicable to Each Theory of Recovery.

i) 1917 Statute. The 1917 Statute applied to contribution claims between jointly liable tortfeasors liable under the tort theories of negligence and strict liability, but not to mixed theory cases involving the statutory contract action of breach of warranty.

ii) 1973 Statute. The 1973 Statute and its comparative negligence and contribution scheme applied only to negligence actions. Therefore, contribution claims involving cases where the defendants were held liable only on theories of negligence and strict liability were governed by the equal apportionment contribution scheme of the 1917 Statute and did not have the benefit of the comparative negligence apportionment scheme of the 1973 Statute. In *General Motors Corp. v. Simmons*, the Texas Supreme Court concluded that the 1917 Statute, rather than the 1973 Statute, applied to cases in which one of the defendants was strictly liable. *General Motors Corp. v. Simmons*, 558 S.W.2d 855, 861-63 (Tex. 1977).

iii) No Statutory Framework for Mixed Theory Recovery Cases. There existed no statutory or judicial framework within which to compare the fault or causation to permit contribution in mixed theory cases where one or more of the defendants were held liable on all three theories: negligence, strict liability and breach of warranty. The legislature failed to rectify the system. *See* Comment, *Duncan v. Cessna Aircraft Co.: "Sooner or Later" Is Now*, 36 BAYLOR L. REV. 429, 457-59 (1984).

(2) *Duncan v. Cessna Aircraft*. In *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984) the supreme court felt compelled to enact its own comparative and contribution scheme due to the continued inaction of the Texas Legislature. The court adopted the state's first common law contribution scheme.

Duncan involved a claim for contribution or indemnity by a strictly liable manufacturer against the allegedly negligent pilot for the damages suffered by a passenger in the plane. The court overruled *General Motors Corp. v. Simmons* and held that the 1917 Statute did not apply to contribution actions involving products liability claims and the possibility of having to compare the negligence, strict liability and breach of warranty actions of co-defendants. The court reasoned that the drafters of the 1917 Statute could not have intended that the 1917 Statute's equal apportionment contribution rule would apply to the multiple theories of recovery and loss allocation problems that courts had encountered in products liability cases. The court also found support in the Texas Legislature's adoption of the 1973 Statute as favoring a Comparative Responsibility Apportionment Scheme. *Id*. 427-28.

(a) Scope of *Duncan's* Comparative Responsibility Apportionment Scheme. The court-made Comparative Responsibility Apportionment Scheme of *Duncan* was subsequently replaced by the 1987 Statute. The *Duncan* Comparative Responsibility and Apportionment Scheme therefore applies to any products case tried after July 13, 1983 and filed before September 1, 1987, in which the fact finder assigns liability to one of the jointly liable defendants on a theory other than negligence.

(b) A Pure Comparative Causation Scheme. The *Duncan* scheme compares "causation" rather than fault, because strict liability and breach of warranty actions do not involve the assessment of fault, and causation is a common element to strict liability, breach of warranty and negligence actions. The *Duncan* scheme is regarded as a "pure" Comparative Causation Scheme since it possesses the elements outlined below. *See* Edgar and Sales, 4 TORTS AND REMEDIES, Ch. 102, § 102.05[3][a] (1991).

i) Plaintiff Able to Recover Even Though Plaintiff's Contributory Negligence is Greater Than 50%. Under the *Duncan* scheme, the plaintiff's damages are reduced by the percentage of negligence attributable to the plaintiff and the plaintiff is allowed to recover from the defendants even though the plaintiff's contributory negligence exceeds the combined causation of the defendants. [Compare to the 1973 Statute which would bar recovery in the event the plaintiff's negligence exceeds the combined negligence of all defendants; also compare to the 1987 Statute and

its Comparative Responsibility and Apportionment Scheme which bars recovery in a strict liability or breach of warranty action if the plaintiff's percentage of responsibility is 60% or more; former TEX. CIV. PRAC. & REM. CODE ANN. § 33.001(b) and the 1995 Proportionate Responsibility Statute which bars recovery if the plaintiff is 51% responsible for the harm, whether by negligent act or omission, by any defective or unreasonably dangerous product, by other conduct or activity that violates an applicable legal standard, or by any combination of these; § 33.003 of the 1995 Proportionate Responsibility Statute.]

ii) Joint and Several Liability. Under the *Duncan* Comparative Causation Scheme, each defendant to whose product the jury attributes any degree of causation is jointly and severally liable for the full amount of the plaintiff's award. [Compare to the 1973 Statute which limited a defendant's liability to said defendant's percentage of negligence in cases where such defendant's liability was less than the plaintiff's share of contributory negligence; also compare to the 1987 Statute providing for a defendant's joint and several liability in cases where the defendant's percentage is more than 10% and plaintiff's percentage is zero, or where defendant's percentage is more than 20% and plaintiff's percentage is less than 60%; TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(b),(c) (Vernon Supp. 1996); and the 1995 Proportionate Responsibility Statute which imposes joint and several liability only in cases where the liable defendant is greater than 50% responsible for the harm; § 33.013(b) of the 1995 Proportionate Responsibility Statute.]

(3) *Bonniwell v. Beech Aircraft*. In *Bonniwell v. Beech Aircraft Corp.*, 663 S.W.2d 816, 819 (Tex. 1984) the Texas Supreme Court held that it had "impliedly abolished the common law doctrine of indemnity between joint tortfeasors in strict liability cases" in *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414, 432 (Tex. 1984).

5. 1987 Statute and Apportionment Under the Comparative Responsibility and Apportionment Scheme. In 1987, the Texas Legislature enacted "tort reform" amendments to the Civil Practice and Remedies Code. TEX. CIV. PRAC. & REM. CODE ANN. §§ 33.001-.016 (Vernon Supp. 1996). *See* Parsons, *Contribution and Indemnity in Texas: Seven Years after Tort Reform*, INSURANCE LAW SEMINAR (UNIV. HOU. 1994); Tade, *Indemnification - Who Wins, Who Loses Under Texas, Louisiana and Maritime Law*, 20TH ANNUAL OIL, GAS & MINERAL LAW INSTITUTE (UNIV. TEX. 1994); Zummo, *Contribution, Indemnification and Complex Settlement Issues*, BUSINESS DISPUTES THROUGH CHANNELS OF DISTRIBUTION (STATE BAR OF TEXAS PDP 1994); Holman, *Contribution and Indemnity*, 1994 ADVANCED CIVIL TRIAL LAW SEMINAR (CORPUS CHRISTI BAR ASS'N 1994); Sanders and Joyce, *"Off to the Races": The 1980's Tort Crisis and the Law Reform Process*, 27 HOU L. REV. 207, 263 (1990); Phifer, *Contribution and Indemnity*, HANDLING INSURANCE AND TORT CLAIMS SEMINAR (UNIV. HOU. 1991); Watson, *Comparative Responsibility Under the New Civil Justice Legislation*, 51 TEX. B.J. 688 (1988); Steenson, *Recent Legislative Responses to the Rule of Joint and Several Liability*, TORT & INS. L.J. 482, 493 (1988); Montford and Barber, *1987 Texas Tort Reform: The Quest for a Fairer and More Predictable Texas Civil Justice System: Part One*, 25 HOU. L. REV. 59, 60 (1988).

a. Applicability. The Comparative Responsibility Apportionment Scheme applies to all tort cases filed on or after September 2, 1987 (except for certain enumerated actions) and prior to the effective date of the 1995 Proportionate Responsibility Statute.

(1) Section 33.001. Section 33.001 of the 1987 Statute provided that the Comparative Responsibility Apportionment Scheme is applicable to the following actions:

(a) Strict Liability or Breach of Warranty. The 1987 Statute provided that it was applicable to actions for personal injury, property damage, or death and in which at least one defendant is found liable on a basis of "strict tort liability, strict products liability, or breach of warranty under Chapter 2, Business and Commerce Code." forms § 33.001(b) (Historical and Statutory Notes Vernon 1997).

(b) Negligence. The 1987 Statute provided that it was applicable to negligence cases which include cases involving

i) damages for personal injury, property damage, or death, § 33.001(a) (Historical and Statutory Notes Vernon 1997); and

ii) cases seeking damages for economic loss, § 33.001(c) (Historical and Statutory Notes Vernon 1997), including but not limited to "negligence relating to any professional services rendered by an architect, attorney, certified public accountant, real estate broker or agent, or engineer ... ."

(2) Exclusions. The 1987 Statute was not applicable to the following types of actions:

(a) Intentional Torts. Section 33.002(a) (Historical and Statutory Notes Vernon 1997).

(b) Exemplary Damage Claims. Claims for exemplary damages included in an action to which the statute otherwise applies. TEX. CIV. PRAC. & REM. CODE ANN. § 33.002(a) (Historical and Statutory Notes Vernon 1997).

(c) Workers' Compensation Claims. Actions to collect workers' compensation benefits or actions against an employer for exemplary damages arising out of the death of an employee. § 33.002(b)(1) (Historical and Statutory Notes Vernon 1997). *See Otis Elevator Co. v. Joseph*, 749 S.W.2d 920 (Tex. App.-- Houston [1st Dist.] 1988, *no writ*)-employee's 65% negligence not a bar or offset to recovery for wrongful death and exemplary damages for employer's gross negligence as to claims arising under Workers' Compensation Act, TEX. LABOR CODE § 406.033 (Vernon 1996) repealing 8308-3.04 (repealed 1993) and formerly Art. 8306, § 3(a), TEX. REV. CIV. STAT. ANN. (Vernon 1986).

(d) DTPA. Certain actions under the Texas DTPA (SubChapter E, Chapter 17, Texas Business & Commerce Code), except as otherwise provided in § 17.50 of the DTPA. TEX. CIV. PRAC. & REM. CODE ANN. former § 33.002(b) (Historical and Statutory Notes Vernon 1997); *see* TEX. BUS. & COMM. CODE ANN. § 17.50(b)(1) (Vernon 1997).

(e) Insurance Code. Actions against insurers for unfair practices under Chapter 21 of the Texas Insurance Code. TEX. CIV. PRAC. & REM. CODE ANN. former § 33.002(b)(3) (Historical and Statutory Notes Vernon 1997).

b. Comparative Responsibility and Apportionment Defined. Under the 1987 Statute the conduct of each claimant, each defendant, and each settling party is to be compared by the trier of fact who determines each person's "percentage of responsibility." The "percentage of responsibility" was defined as follows:

> ... that percentage attributed by the trier of fact to each claimant, each defendant, or each settling person with respect to causing or contributing to cause in any way, whether by negligent act or omission, by any defective or unreasonably dangerous product, by other conduct or activity violative of the applicable legal standard, or by any combination of the foregoing, the personal injury, property damage, death, or other harm for which recovery of damages is sought.

TEX. CIV. PRAC. & REM. CODE ANN. § 33.011 (Vernon Supp. 1996).

c. Tort Reform Limitation on Joint and Several Liability. The common law principle of joint and several liability for the damages resulting from an "indivisible wrong or tort" was replaced under the 1987 Statute with the "tort reform" concept that a defendant is generally liable "only for the percentage of the damages found by the trier of fact equal to that defendant's percentage of responsibility with respect to the personal injury, property damage, death, or other harm for which the damages are allowed." TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(a) (Vernon 1997).

d. Exceptions in Which Joint and Several Liability Still Imposed. The 1987 Statute however allowed significant exceptions to the this limitation on joint and several liability.

(1) Pure Negligence Case. In a case in which all defendants are liable for negligence, none for strict liability, joint and several liability results for the defendants with the following percentages of comparative responsibility:

(a) Defendants With Greater than 20% Responsibility and Greater than Claimant's Percentage. In cases where a defendant's percentage of responsibility is more than 20% and that percentage is greater than the percentage of responsibility attributed to the claimant, the defendant is jointly and severally liable for the plaintiff's damages. TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(b) (Historical and Statutory Notes Vernon 1997). *C&H Nationwide, Inc. v. Thompson*, 810 S.W.2d 259, 275 (Tex. App.--Houston [1st Dist.] 1991), *aff'd in part and rev'd in part*, 1994 WL 278167.

Example: Plaintiff sues defendant 1 and defendant 2. The jury finds both defendants liable based upon negligence. There are no findings of strict liability or breach of warranty. The jury finds the plaintiff is 25% responsible, defendant 1 is 50% responsible, and defendant 2 is 25% responsible.

The case is a pure negligence case. There is no bar to recovery because the plaintiff is less than 51% responsible. The plaintiff's recovery will however be reduced by 25%. Defendant 1 is jointly and severally liable, since defendant 1 is more responsible than the plaintiff and is over 20% responsible. Defendant 2 is more than 20% responsible, but is not more responsible than the plaintiff; therefore defendant 2 is not jointly and severally liable.

The above example and the other examples contained in this discussion of the 1987 Statute are contained in Watson, *Comparative Responsibility Under the New Civil Justice Legislation*, 51 TEX. B.J. 688 (1988).

(b) Innocent Plaintiff *and* Defendant Greater than 10% Responsible. In cases where a defendant's percentage of responsibility is more than 10% and no percentage of responsibility is attributed to the claimant, the defendant is jointly and severally liable for the claimant's damages. TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(c) (Historical and Statutory Notes Vernon 1997).

Example: Plaintiff sues defendant 1 and defendant 2. The jury finds both defendants liable for negligence, and there are no findings of strict liability or breach of warranty. The jury finds the plaintiff is zero percent responsible, defendant 1 is 80 percent responsible, and defendant 2 is 20% responsible.

The case is a pure negligence case. The plaintiff is not barred from recovery, and recovery is not reduced. Defendant 1 is more responsible than plaintiff and more than 20% responsible; therefore defendant 1 is jointly and severally responsible. Defendant 2 is more responsible than the plaintiff, but not "more than 20% responsible," but is still jointly and severally liable because he is more than 10% responsible and the plaintiff is not responsible. However, if defendant 2 had only been 10% responsible, he would not have been jointly and severally liable.

(2) Mixed Case with Strict Liability or Breach of Warranty With Threshold Levels of Comparative Responsibility. Joint and several liability is imposed on defendants in cases in which at least one defendant is found liable on a theory of strict tort liability, strict products liability, or breach of commercial warranty if the following thresholds of comparative liability exist:

(a) Defendants with Greater than 20% Responsibility. Defendants with greater than 20% responsibility. TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(b) (Historical and Statutory Notes Vernon 1997).

Example: Plaintiff sues defendant 1 and defendant 2. The jury finds both defendants liable based upon strict liability. The jury finds the plaintiff is 20% responsible, defendant 1 is 50% responsible and defendant 2 is 30% responsible.

The case is a strict liability case. The plaintiff is not barred from recovery because the plaintiff is less than 60% responsible. However, the plaintiff's recovery is reduced by the 20% he is found to be responsible. Although the general rule is "no joint and several liability," since each defendant is over 20% liable, each defendant is jointly and severally liable.

(b) Innocent Claimant *and* Defendant Greater than 10% Responsible. If the percentage of responsibility of the defendant is more than 10% and the claimant's percentage of responsibility is zero. TEX. CIV. PRAC. & REM. CODE ANN. § 33.013(c) (Historical and Statutory Vernon 1997).

Example: Plaintiff sues defendant 1 and defendant 2. The jury finds defendant 1 and defendant 2 liable for negligence and strict liability. The jury finds the plaintiff is 1% responsible, defendant 1 is 79% responsible and defendant 2 is 20% responsible.

The case is a mixed case. There is no bar to recovery and the plaintiff's recovery will be reduced by 1%. The "over 20 percent" exception to the no joint and several liability rule applies to defendant 1. Neither the "over 20% exception" nor the "over 10% percent" exception apply to defendant 2.

(3) Toxic Torts. Joint and several liability results if the death, personal injury, or property damage results from either (a) the disposition, discharge, or release into the environment of any hazardous substance, or (b) a "toxic tort." TEX. CIV. PRAC. & REM. CODE ANN. §§ 33.013(c)(2)-(3) (Historical and Statutory Notes Vernon 1997). "Toxic torts" are defined in § 33.013(c)(3) as follows:

> ... a cause of action in tort or for breach of implied warranty under Chapter 2, Business & Commerce Code, arising out of exposure to hazardous chemicals, hazardous wastes, hazardous hydrocarbons, similarly harmful organic or mineral substances, hazardous radiation sources, and other similarly harmful substances (which usually, but need not necessarily, arise in the work place), but not including any "drug" as defined in Section 81.001 (3), Civil Practice and Remedies Code.

e. Bars to Recovery. The Comparative Responsibility and Apportionment Scheme of the 1987 Statute provided certain **bars** to recovery if the claimant's comparative responsibility is greater than the following statutory ceilings:

(1) If Only Negligence is Found, the 51% Bar Rule Applies. If only negligence liability was found between the plaintiff and all of the defendants, the plaintiff **may** recover only if the plaintiff's responsibility is 50% or less. TEX. CIV. PRAC. & REM. CODE ANN. § 33.001(a) and (c) (Historical and Statutory Notes Vernon 1997) (referred to as the **"51% Bar Rule"**).

(2) If Strict Liability or Breach of Warranty is Found, the 60% Bar Rule Applies. If at least one defendant was found liable based upon strict product liability or strict tort liability, or breach of UCC warranty, the plaintiff was permitted to recover only if the plaintiff's responsibility was less than 60%. TEX. CIV. PRAC. & REM. CODE ANN. § 33.001(b) (Historical and Statutory Notes Vernon 1997).

(3) If Mixed Liability is Found, the 60% Bar Rule Applies. In cases in which defendants are found liable on a mixed theory of negligence and either strict tort liability or breach of UCC warranty, the plaintiff was permitted to recover only if the plaintiff's responsibility was less than 60%.

(4) Economic Loss Cases Based on Negligence. Economic loss cases based upon negligence are subject to the 51% Bar Rule. TEX. CIV. PRAC. & REM. CODE ANN. § 33.001(c) (Historical and Statutory Notes Vernon 1997).

6. 1995 Proportionate Responsibility Statute. The 74th Texas Legislature has enacted further significant "tort reform" amendments to Chapter 33 of the Civil Practice & Remedies Code (referred to herein as the "1995 Proportionate Responsibility Statute" or the **"1995 Statute"**). Holman, Gallagher and Boudreaux, *Contribution and Indemnity and Complex Settlement Agreements,* INSURANCE LAW SEMINAR D (UNIV. HOU. 1996).

a. Effective Date.

(1) Causes of Action Accruing 9/1/95. The 1995 Statute takes effect on September 1, 1995, and applies to all causes of action that accrue on or after September 1, 1995.

(2) Suits Filed Beginning 9/1/96. The 1995 Statute applies to all causes of action that accrued before the effective date and on which suit is filed on or after September 1, 1996.

(3) Suits Filed Before 9/1/96. Suits filed prior to September 1, 1996 are governed by the law in effect prior to September 1, 1995.

b. Applicability. The 1995 Proportionate Responsibility Statute is applicable to any cause of action based on tort. § 33.002 of the 1995 Statute.

(1) Inclusive Scope. The inclusive nature of the 1995 Statute is indicated by § 33.003--"Determination of Percentage of Responsibility" which provides that

> The trier of fact, as to each cause of action asserted, shall determine the percentage of responsibility, stated in whole numbers, for the following persons with respect to each person's causing or contributing to cause in any way the harm for which recovery of damages is sought, whether by negligent act or omission, by any defective or unreasonably dangerous product, by other conduct or activity that

violates an applicable legal standard, or by any combination of these: ..."

Section 33.002 of the 1995 Statute deleted the provisions of § 33.002 of the 1987 Statute that excluded from the applicability of the statute actions brought under the DTPA, Chapter 17E, TEX. BUS. & COMM. CODE [§ 33.002(b)(2) exclusion eliminated] or under Chapter 21 of the INSURANCE CODE [§ 33.002(b)(3) eliminated].

(2) Proportionate Responsibility. The 1995 Statute continues the "tort reform" scheme of § 33.013(a) "Amount of Liability" unchanged. Section 33.013(a) provides that

> Except as provided in Subsections (b) and (c), a liable defendant is liable to a claimant only for the percentage of the damages found by the trier of fact equal to that defendant's ***percentage of responsibility*** with respect to the personal injury, property damage, death, or other harm for which the damages are allowed.

This is the general rule apportioning liability in accordance with each liable defendant's responsibility.

(3) Exclusion from 1995 Statute's Limits on Joint and Several Liability. The 1995 Statute allows for "joint and several liability" in the following limited cases:

(a) Defendants With Greater than 50% Responsibility. Section 33.013(b) of the 1995 Statute amended the 1987 Statute to raise the threshold for the imposition of joint and several liability from 10% responsibility to "greater than 50%" responsibility. A liable defendant who the trier of fact determines is greater than 50% responsible for the harm, is jointly and severally liable for the damages with other liable defendants.

In raising the threshold for imposition of joint and several liability, the 1995 Statute eliminated the requirement that the responsibility of the defendant in a negligence action be greater than the percentage of responsibility attributed to the claimant due to the 51% Bar Rule.

The 1995 Statute eliminated from the imposition of joint and several liability the provision in the 1987 Statute in § 33.013(c)(1) which imposed joint and several liability in cases where the defendant's percentage of liability was more than 10% and the plaintiff was "innocent" (no percentage of responsibility assessed to the plaintiff).

(b) Toxic Torts Greater than 15% of the Responsibility. Section 33.013(c) of the 1995 Statute imposes joint and several liability on a defendant if the percentage of responsibility attributable to the defendant is "greater than 15%" and is caused by the depositing, discharge, or release into the environment of any hazardous or harmful substance, or if the claimant's personal injury, property damage, death or other harm resulted from a toxic tort.

(c) Penal Code. The 1995 Statute also adds § 33.002(b), providing for joint and several liability for a defendant who, with specific intent to do harm to others, acts in concert with another person to engage in conduct under certain listed Sections of the Penal Code (*e.g.*, § 32.46 securing execution of a document by deception; § 19.02 murder).

c. 51% Bar Rule Applicable to Cases under 1995 Statute. The 1995 Statute provides for a 51% Bar Rule similar to the 1987 Statute. Section 33.001 provides that a "claimant may not recover damages if his percentage of responsibility is greater than 50 percent." The 1995 Statute, however, **eliminates** the distinction previously applicable to mixed theory cases which applied a 60% Bar Rule. The 1987 Statute did not bar a claimant's recovery in a mixed theory case where at least one defendant was found liable based upon strict liability or breach of a UCC warranty, unless the claimant was at least 60% responsible.

B. Statutory Indemnity. In addition to common law indemnity, the legislature has provided for statutorily imposed indemnity in certain relationships. Following is a limited discussion of several of these statutorily imposed indemnities.

1. Electric Companies. TEX. HEALTH & SAFETY CODE ANN. § 752.008 (Vernon 1992) provides electric companies and municipalities which own power lines with a statutory indemnity. Section 752.008 provides that if a person violates the statute by operating equipment (without listed precautions) within six feet of a high-voltage line, that person must indemnify the owner or operator of the line for any damages caused by such violation. *See Hernandez v. Houston Lighting & Power Co.*, 795 S.W.2d 775 (Tex. App.–Houston [14th Dist.] 1990, *no writ*)--workers' compensation claim barred by statutory indemnity. The court in *Olson v. Central Power & Light Co.*, 803 S.W.2d 808 (Tex. App.--Corpus Christi 1991, *writ denied*) held that the statutory indemnity provided by the Texas Public Utilities Act for liabilities incurred by a utility due to a person contacting one of the utility's high voltage lines is not overridden by the provisions of the Texas Workers' Compensation Act, which shields a workers' compensation subscriber from liability to third parties for suits brought against third parties by the subscriber's employees. The court in *Martinez v. Gulf States Utility Co.,* 864 S.W.2d 802 (Tex. App.--Houston [14th Dist.] 1993, *writ denied*) held that a plaintiff's release of a property owner, upon whom § 752.008 imposed a statutory indemnity of the utility company, barred the plaintiff from recovery against the utility company since a *circuit of indemnity* had been created (plaintiff recovers against utility company, utility company recovers against property owner, property owner indemnified by plaintiff).

2. Governmental Employees.

a. Individually as Defendant. TEX. CIV. PRAC. & REM. CODE ANN. § 104.0011 (Vernon 1997) provides a statutory duty on the state to indemnify its employees for actual damages, court costs and attorney's fees.

b. Employees of Texas Department of Mental Health. TEX. HEALTH & SAFETY CODE ANN. § 591.024(b) (Vernon 1992) provides a statutory

indemnity by the state of employees of the Texas Department of Mental Health and Mental Retardation for negligence if the claim arises while the employee is acting in the scope of its authorized duties.

3. Shipper's Indemnity. TEX.BUS.& COM. CODE ANN. § 7.301(e) (Vernon 1991) provides that a shipper shall indemnify a carrier against damage caused by inaccuracies in the description, marks, labels, number, kind, quantity, condition and weight of goods provided by the shipper.

C. Prelude to Discussion of Contractual Indemnity. The foregoing factors have amplified the need to bring certainty into the risk management decisions of contacting parties. The prevalence of indemnification clauses in common contractual arrangements between commercial parties resulted in the development of a special insurance product by the insurance industry to provide insurance coverage for an insured's assumption of the liability of another person. This coverage has been a standard component of commercial general liability insurance policy forms promulgated by the Insurance Services Offices, Inc. ("***ISO***"), since 1986. Prior to that time, contractual liability coverage was readily available by endorsement to the 1973 policy.

II. Contractual Indemnity.

A. Distinguished from Guaranty and Suretyship. Both guaranty and surety agreements are collateral undertakings dependent upon the existence of another contract or transaction. *Pham v. Mongiello,* 58 S.W.3d 284 (Tex.App.-Austin [3rd Dist.] 2001, *no writ*)- court found that rules governing guarantees should be analogous to rules governing indemnity agreements; a guaranty of a tenant's obligations should clearly set out what possible charges could be incurred by the tenant, for example, charges arising out of a tenant's negligence. Indemnification is an original undertaking between the Indemnifying Person and the Indemnified Person. An indemnification may be executed in connection with another contract, as in the case of a subcontractor's indemnity protecting a contractor in connection with contractor's construction contract with the property owner. *See* 14 TEX. JUR. 3d *Contribution and Indemnification* § 2 *Distinctions* 477 (1997).

1. Indemnity.

a. "Liabilities" or "Damages". Indemnities have sometimes been classified as an "indemnity against liability." *Russell v. Lemons,* 205 S.W.2d 629, 631 (Tex. Civ. App.--Amarillo 1947, *writ ref'd n.r.e.*). In the case of a promise to indemnify against liability, a cause of action accrues to the indemnified person only when the liability has become fixed and certain, as by rendition of a judgment. Possibility that liability triggering indemnity will be incurred in pending action is a "future hypothetical event" within meaning of rule that Uniform Declaratory Judgments Acts gives court no power to pass upon hypothetical or contingent situations. *Boorhem-Fields, Inc. v. Burlington Northern Railroad Co.,* 884 S.W.2d 530 (Tex. App.--Texarkana 1994, *no writ*); § 37.001 TEX. CIV. PRAC. & REM. CODE ANN. (Vernon 1997).

Alternatively, an indemnity may be an "indemnity against damages." With respect to a promise to indemnify against damages, a right to bring suit does not accrue until the indemnified person has suffered damage or injury by being compelled to pay the judgment or debt. *Holland v. Fidelity & Deposit Co. of Maryland*, 623 S.W.2d 469, 470 (Tex. App.--Corpus Christi 1981, *no writ*).

b. Contractual Obligations or Torts. Indemnity agreements may cover contractual obligations of others or torts committed by others.

(1) Contractual Obligations. For example, it is not against public policy for a withdrawing officer to indemnify a purchasing shareholder for I.R.S. penalties subsequently imposed on a corporation and its shareholders. *Tubb v. Bartlett,* 862 S.W.2d 740, 751 (Tex. App.--El Paso 1993, *writ denied*). Also, an indemnity can cover **economic damages** to arise in the future to third persons due to the contractual arrangements between contract parties. Such indemnities are not governed by the express negligence or similar doctrine (if they do not involve indemnification against one's future negligence). *Transcontinental Gas Pipeline Corp. v. Texaco,* 35 S.W.3d 658 (Tex.App.-Houston [1st Dist.] 2000, *no writ*). However, shifting of risk from one contracting party to another contracting party is neither an indemnity nor a release and need not meet the fair notice and express negligence tests otherwise applicable to *"extraordinary"* shifting of risk. *Green International v. Solis*, 951 S.W.2d 384 (Tex. 1997) ("**no-damages-for-delay**" provision in a construction contract that shifted to a subcontractor the economic damages arising out of the risk of a project's delay was enforceable by the contractor, even though the contractor may have caused the delay, if the potential for delay was contemplated by the parties, or if the delay was not for an unreasonable period of time that would justify the subcontractor in abandoning the contract, or if the contractor did not engage in active interference or wrongful conduct).

Perhaps the result might have been different in *Griffin Indus. v. Foodmaker, Inc.*, 22 S.W.3d 33 (Tex.App.-Houston [14th Dist.]2000, *no writ*) involving an injury to an employee of Foodmaker a/k/a Jack in the Box if the indemnity had covered damages arising out of its breach of contract. In *Foodmaker* there was some evidence that Griffin did not respond to service calls to fix a grease receptacle that it furnished Foodmaker. A Foodmaker employee was injured when he slipped on a greasy ladder attempting to pour hot french fry grease into a ventilator slot 6'10" above the ground. The proper slot was broken. The court said,

> Assuming, without deciding, that Griffin did not respond to one or more service requests in a timely manner, such conduct might constitute a breach of its service contract with Foodmaker but it is not evidence of negligence. The duty to pick up the grease stems solely from the parties' contract.

(2) Torts.

(a) Negligence. Indemnity against "one's own negligence" has long been recognized in Texas. *See* the discussion of the "express negligence test" as a rule of contract construction below. *Ohio Oil Co. v. Smith*, 365 S.W.2d 621, 624 (Tex. 1963); *Ethyl Corp. v. Daniel Const. Co.,* 725 S.W.2d 705 (Tex. 1987). In *Atlantic Richfield Co. v. Petroleum Personnel, Inc.,* 768 S.W.2d 724 (Tex. 1989), the Texas Supreme Court held that the language of the contractual indemnity provision satisfied the express negligence test even though it did not differentiate between "degrees of negligence." Certain "magic" words like "active," "passive," "sole," "joint," or "concurrent" to describe the degrees of negligence covered were not necessary. The court determined that "any negligent act or omission of ARCO" was sufficient to define the parties' intent. *Id.* at 726.

Perhaps what is more important is to determine what degree of negligence is excluded from the indemnity. *E.g.,* "but not injuries due to the sole negligence of the _____ (*e.g.,* landlord)."

(b) Gross Negligence and Punitive Damages. In *Atlantic Richfield Co. v. Petroleum Personnel, Inc.,* 768 S.W.2d 724 (Tex. 1989), the Texas Supreme Court observed, in a footnote to the opinion, that it was **not deciding** whether indemnity for one's own gross negligence or intentional injury may be contracted for or awarded by Texas

courts. The court stated that "[p]ublic policy concerns are presented by such an issue ... ." *Id.* at 726 n.2. Texas allows insurance coverage for punitive damages derivative of gross negligence. *American Home Assur. Co. v. Safway Steel Products Co.,* 743 S.W.2d 693 (Tex. App.--Austin 1987, *writ denied*); *Home Indemnity Co. v. Tyler,* 522 S.W.2d 594 (Tex. App.--Houston [14th Dist.] 1975, *writ ref'd n.r.e.*). Recently, the San Antonio court of appeals held that an indemnity for one's own negligence also **included** all shades and degrees of negligence, including one's own gross negligence. *Webb v. Lawson-Avila Const., Inc.,* 911 S.W.2d 457 (Tex. App.--San Antonio 1995, *writ dism'd by agreement*).

Also see Sieber & Calicutt v. La Gloria, 66 S.W.3d 340 (Tex.App. [12th Dist.] 2001, *no writ*) where the court assumed without discussion that negligence of the Indemnified Party included its gross negligence.

(c) Intentional Torts. The issue of the enforceability of an indemnity for an intentional tort (Tenneco's misappropriation and improper use of confidential information obtained in bidding process) was raised in *Tenneco Oil Co. v. Gulsby Engineering, Inc.,* 846 S.W.2d 599 (Tex. App.--Houston [14th Dist.] 1993, *writ denied*). However, the court of appeals was able to sustain the trial court's summary judgment in favor of Tenneco on the grounds that the indemnity provision in the contract with Gulsby Engineering specifically covered patent infringement suits, and therefore included Tenneco's and Gulsby's joint and several liability for having infringed the unsuccessful bidder's patent.

2. Guaranty. A guaranty agreement is expressly for the benefit of the third party (the creditor). The guarantor covenants to pay the debt of the debtor in the event of the debtor's default. Indemnification involves a promise to the liable party to reimburse such person if it is compelled to pay a debt.

3. Suretyship. The surety in a suretyship agreement makes a direct promise to perform the principal's obligation if the principal fails to perform.

a. Suretyship Supported by Implied Contract of Indemnity. Many suretyship agreements are supported by an "implied contract of indemnity" wherein the principal impliedly indemnifies the surety. *See* for example *Felker v. Thomas*, 83 S.W.2d 1055 (Tex. Civ. App.–El Paso 1935, *no writ*)--permitting an accommodation maker on a vendor's lien note to recover on an implied contract of indemnity against the accommodated party upon foreclosure of the vendor's lien; *also see Navarro Oil Co. v. Cross*, 200 S.W.2d 616 (Tex. 1946).

b. Suretyship Supported by Express Contract of Indemnity. Most suretyship agreements are accompanied by an express indemnity agreement. *See Central Surety & Ins. Corp. v. Martin*, 224 S.W.2d 773 (Tex. Civ. App.--Beaumont 1949, *writ ref'd*); Forms: Indemnification of Surety, 9 AM. JUR. LEGAL FORMS, 2d, *Indemnity* § 142:23 (1985).

B. Indemnity Against One's Own Negligence.

1. Background.

a. Prior to 1971 Generally-Worded and Broad Statements of Indemnity.

(1) Not Violative of Public Policy. As a general proposition, contractual indemnity provisions have long been held not to violate the public policy of the state of Texas. *Ohio Oil Co. v. Smith*, 365 S.W.2d 621, 624 (Tex. 1963). The adoption by the Texas Supreme Court of various contract interpretation rules, such as the "clear and unequivocal rule" or the "express negligence test," are reaffirmations of this basic proposition.

(2) Statements Sufficiently Broad to Include Negligence Rule. Prior to 1971, a broad general statement regarding indemnity for any injury or death of any persons or damage to property resulting from the use of equipment was effective against the Indemnifying Person. *James Stewart & Co. v. Mobley*, 282 S.W.2d 290 (Tex. Civ. App.--Dallas 1955, *writ ref'd*).

Under this rule, an indemnity contract was sufficiently worded to pass liability to the Indemnifying Person when it was sufficiently broad as to cover the negligence of the indemnified person and it was clear that the intent was to do so. *Spence & Howe Const. Co. v. Gulf Oil Corp.*, 365 S.W.2d 631 (Tex. 1963); *Alamo Lumber Co. v. Warren Petroleum Corp.*, 316 F.2d 287, 290-91 (5th Cir. 1963).

b. 1971-1987 Clear and Unequivocal Standard.

(1) Broad Statements No Longer Sufficient Unless Obligation Expressed in Clear and Unequivocal Terms.

(a) *McCann Construction*. In 1971, the Texas Supreme Court made a significant change in indemnity contract law. Broad, general indemnity provisions would no longer suffice to protect an indemnified person against the consequences of its own negligence. In *Joe Adams & Son v. McCann Const. Co.*, 475 S.W.2d 721 (Tex. 1971), the Texas Supreme Court held that an indemnity agreement will not protect the indemnified person against the consequences of his own negligence unless the obligation was expressed in unequivocal terms. In holding that the indemnity agreement in question did not protect the indemnified person, the court stated:

> It is not necessary for the parties to say, in so many words, that they intend to save the indemnitee harmless from liability for his own wrongs, but it is necessary for that intention to clearly appear when all the provisions of the contract are considered in light of the circumstances surrounding its execution.

Provision: The indemnity provision construed by the court is as follows:

> The Contractor (Adams) shall effectually secure and protect its work and shall bear and be liable for all loss or damages of any kind which may happen to

the work or any materials to be incorporated therein at any time prior to the final completion and acceptance thereof. McCann Construction ... shall not be responsible for any damage done to the work or property of the Contractor, unless such damage shall be caused by the direct negligence of McCann Construction. ...

> The Contractor shall protect, indemnify and save McCann Construction ... and Owner harmless from any and all claims, suits, and actions of any kind or description, for damage or injuries to persons or property received or sustained by any party or parties through or on account of any act or in connection with the work of the Contractor or its agents or servants or subcontractors, or any default or omission of the Contractor, or its agents or servants or subcontractors in the performance of this contract, or through the use of improper or defective materials or tools or on account of injury of damage to adjacent buildings or property occasioned by work under this contract, or through failure to give the usual requisite and suitable notices to all parties, whose persons, estates or premises may be, in any way, interested in or affected by the performance of this work, and at its own cost shall defend any and all suits or actions that may be brought against McCann Construction... or Owner by reason thereof, and in the event of the failure of the Contractor to defend such suits McCann Construction... shall have the right and power to defend same and charge all costs of such defense to the Contractor or its Surety. (Emphasis added by author.)

While the "clear and unequivocal" rule appeared to be simple and straight forward, it was not easy in its application and only a small number of indemnity provisions were judicially enforced to protect the indemnified person against its own conduct. *See* Scheer, *The Contractual Indemnity Provision Effective to Protect an Indemnitee Against His Own Negligence or Other Fault*, 17 TEX. TECH L. REV. 845, 856-874 (1986).

(b) *Fireman's Fund*. In *Fireman's Fund Insurance Co. v. Commercial Standard Indemnity Co.*, 490 S.W.2d 818 (Tex. 1972), the Texas Supreme Court established the "clear and unequivocal" standard. The majority of the court attempted to define this stricter standard:

> (w)e have, in fact, progressed toward the so-called "express negligence" rule as near as is judicially possible without adopting it.

Id. at 822. The court, however, failed to define the stricter standard.

Provision: The indemnity provision construed by the court read as follows:

> All Contractors shall be responsible each for his work and every part thereof, and for all materials, tools, appliances and property of every description used in connection therewith, (in case of general contract, General Contractor assumes entire responsibility). They shall specifically and distinctly assume and do so assume all risks of damage or injury from any cause except negligence of Owner, its officers, agents and employees, to property or persons used or employed on or in connection with the work, and of all damage or injury to any persons or property wherever located, resulting from any action or operation under the contract or in connection with the work, and undertake and promise to protect and defend the Owner and Architect-Engineer against all claims on account of any such damage or injury. (Italicized emphasis added by court; underlining added by author.)

Id. at 821.

The court found that this broad language of "protecting ... the Owner ... against all claims" did not clearly and unequivocally indicate an intent to indemnify the owner (General Motors) from its own negligence.

(2) Exceptions to Rule. The *Fireman's Fund* Court recognized three exceptions to the "clear and unequivocal rule." The court found the types of agreements outlined below did not require a provision which unequivocally protected an indemnified person against the indemnified person's own negligence. *Also see* review of the exceptions in *Gulf Coast Masonry, Inc. v. Owens- Illinois, Inc.*, 739 S.W.2d 239 (Tex. 1987).

(a) Premises Defects or Maintenance. Agreements in which one person clearly undertook to indemnify another person against liability for injuries or damages resulting from defects in certain premises or from the maintenance or operation of a specified instrumentality. *Mitchell's, Inc. v. Friedman*, 303 S.W.2d 775 (Tex. 1957). The supreme court later held that this situation was not a true exception, but merely constituted an application of the general rule and required a finding that the provision satisfied the clear and unequivocal test. *Eastman Kodak Co. v. Exxon Corp.*, 603 S.W.2d 208, 212 (Tex. 1980).

(b) Complete Supervision of Property or Persons. Agreements which related to situations in which the Indemnifying Person had complete supervision over the property and employees of the indemnified person in connection with the performance of the Indemnifying Person's obligations under the contract. *Spence & Howe Const. Co. v. Gulf Oil Corp.*, 365 S.W.2d 631 (Tex. 1963). This exception was never applied after its recognition in *Fireman's Fund.*

(c) Complete Indemnity Agreement. Agreements in which there was an unequivocal provision that the Indemnifying Person would indemnify the indemnified person from all liability by reason of injury to the indemnified person's employees. *Ohio Oil Co. v. Smith*, 365 S.W.2d 621 (Tex. 1963). This exception was applied twice: *Richmond v. Amoco Production Co.*, 390 F. Supp. 673, 676-677 (E.D. Tex. 1975), *aff'd without opinion*, 532 F.2d 1373 (5th Cir. 1976); and *Eastex Inc. v. Stebbins Engineering & Mfg. Co.*, 436 F. Supp. 577 (E.D. Tex. 1977).

(3) Cases. *Amoco Chemicals Corp. v. Sutton*, 551 S.W.2d 459 (Tex. Civ. App.--Eastland 1977, *writ ref'd n.r.e.*). The supreme court held the following provision met the clear and unequivocal test:

Provision:

> Contractor shall ... indemnify Company ... from and against any and all loss, costs, damage, expense, claims, suits and liability on account of any and all damage to, or loss or destruction of any person ... arising directly or indirectly out of, or in connection with the performance of this Contract whether caused by a negligent act or omission of either party hereto, or their employees, or otherwise, except that Contractor assumes no liability for the sole negligent acts of Company, its agents, servants or employees. (Emphasis added by author.)

The "clear and unequivocal" rule was confirmed by the Texas Supreme Court as recently as 1986 in *Dorchester Gas Corp. v. American Petrofina, Inc.*, 710 S.W.2d 541, 543 (Tex. 1986).

2. Express Negligence Doctrine Adopted in 1987.

a. *Ethyl*.

(1) Case. The Texas Supreme Court in *Ethyl Corp. v. Daniel Const. Co.*, 725 S.W.2d 705 (Tex. 1987) held an indemnity provision to be **unenforceable** because it did not specifically state that the contractor (Daniel) would indemnify Ethyl for Ethyl's own negligence.

In *Ethyl*, an employee of the contractor was injured while working on a construction project for the owner. After the employee settled his claim for workers' compensation benefits, the employee sued the owner who, in turn, sued the contractor (employer) seeking indemnity. The jury found the owner 90% negligent and the contractor 10% negligent. The owner sued the contractor for indemnification on the following indemnity provision:

Provision:

> Contractor (Daniel) shall indemnify and hold Owner (Ethyl) harmless against any loss or damage to persons or property as a result of operations growing out of the performance of this contract and caused by the negligence or carelessness of Contractor, Contractor's employees, subcontractors and agents or licensees. (Emphasis added by author.)

(a) Ethyl's Negligence Not Covered. Ethyl argued that the language "any loss" and "as a result of operations growing out of the performance of this contract" expressed the contractor's intent to cover Ethyl's negligence.

In holding that *Ethyl* was **not entitled** to indemnification by the contractor, the court stated

> parties seeking to indemnify the indemnitee from the consequences of its own negligence must express that intent in specific terms. Under the doctrine of express negligence, the intent of the parties must be specifically stated within the four corners of the contract.

The court stated the following policy for the new standard:

> As we have moved closer to the express negligence doctrine, the scriveners of indemnity agreements have devised novel ways of writing provisions which fail to expressly state the true intent of those provisions. The intent of the scriveners is to indemnify the indemnitee for its negligence, yet be just ambiguous enough to conceal that intent from the indemnitor. The result has been a plethora of law suits to construe these ambiguous contracts. We hold the better policy is to cut through the ambiguity of those provisions and adopt the express negligence doctrine.

Id. at 707-08.

(b) Daniel's Negligence Not Covered. The supreme court also rejected Ethyl's interpretation that the indemnity clause indemnified Ethyl against Daniel's 10% concurring negligence. After the court rejected Ethyl's claim for indemnification for Ethyl's 90% negligence, Ethyl sought contribution or indemnification for Daniel's 10%. The court termed this claim as one for **"comparative indemnity."** The court held that the indemnity provision **did not meet** the express negligence test in this respect. The court stated

> Indemnitees seeking indemnity for the consequences of their own negligence which proximately causes injury jointly and concurrently with the indemnitor's negligence must also meet the express negligence test. ... Parties may contract for comparative indemnity so long as they comply with the express negligence doctrine set out herein.

Id. at 708-09. The court of appeals had disposed of the same argument by stating that the 1973 Statute (Art. 2212a) did not create a right of contribution or indemnity against the employer (independent of a contractual indemnity) and cited *Varela v. American Petrofina Co. of Texas, Inc.*, 658 S.W.2d 561 (Tex. 1983). *Daniel Const. Co. v. Ethyl Corp.*, 714 S.W.2d 51, 54 (Tex. App.--Houston [14th Dist.] 1986).

(2) Effect of *Ethyl*. The court overruled the clear and unequivocal standard as well as the three exceptions to the standard listed in *Fireman's Fund.* The court applied the new standard retroactively thereby calling into question most previously drafted indemnity agreements. Arguably, the *Ethyl* provision did not even satisfy the "clear and unequivocal test" since the provision did not mention protecting the Indemnified Person, clearly and unequivocally or otherwise, from liability for the Indemnified Person's own negligence. Provisions so constructed had previously been held not to satisfy the clear and unequivocal test. *Delta Drilling Co. v. Cruz*, 707 S.W.2d 660, 668 (Tex. App.--Corpus Christi 1986, *writ ref'd n.r.e.*).

b. Cases Applying *Ethyl*.

(1) Supreme Court Decisions.

(a) *Singleton*. In *Singleton v. Crown Central Petroleum Corp.*, 729 S.W.2d 690 (Tex. 1987), the Texas Supreme Court found that the following provision **failed** the express negligence standard since the provision stated what was not to be indemnified–claims resulting from the sole negligence of the premises owner--rather than expressly stating that the premises owner was to be indemnified from its own negligence.

Provision:

> Contractor agrees to ... indemnify ... owner from and against any and all claims .. of every kind and character whatsoever, ... for or in connection with loss of life or personal injury ... directly or indirectly arising out of ... the activities of contractor ... excepting only claims arising out of accidents resulting from the sole negligence of owner. (Emphasis added by author.)

(b) *Gulf Coast Masonry*. *Gulf Coast Masonry, Inc. v. Owens-Illinois, Inc.*, 739 S.W.2d 239 (Tex. 1987 *per curiam*). In a *per curiam* opinion, and without hearing oral argument, the Texas Supreme Court upheld the trial court's granting summary judgment to the Indemnifying Person (the contractor) on the basis that the **indemnity provision was unenforceable as a matter of law**. The court found the following provision **failed** expressly to indemnify the plant owner for injuries to employees of the contractor due to either party's negligence.

Provision:

> Contractor (Gulf Coast) agrees to indemnify and save owner (Owens-Illinois) harmless from any and all loss sustained by owner ... from any liability or expense on account of property damage or personal injury ... sustained by any person or persons, including but not limited to employees of ... contractor ... arising out of ... the performance or non-performance of work hereunder by contractor ... or by any act or omission of contractor, its subcontractor(s), and their respective employees and agents while on owner's premises .... (Emphasis added by author.)

Although the agreement specifies the contractor's duty to indemnify the owner for claims resulting from the contractor's acts, it fails to state, with equal specificity, the obligation to indemnify for claims resulting from acts of other parties (*i.e.*, owner) and does not expressly refer to the negligence of either the owner or the contractor as an Indemnified Matter.

(c) *ARCO*. *Atlantic Richfield Co. v. Petroleum Personnel, Inc.*, 758 S.W.2d 843, 844 (Tex. App.--Corpus Christi 1988), *rev'd*, 768 S.W.2d 724 (Tex. 1989). In this case, the employee of the contractor (PPI) sued the owner (ARCO) for injuries sustained while working on the owner's drilling platform. ARCO impleaded the contractor seeking indemnification from the contractor under the indemnification provision in the contract between ARCO and the contractor. The Texas Supreme Court found the following provision **met** the express negligence standard:

Provision:

> Contractor (PPI) agrees to hold harmless and unconditionally indemnify company (ARCO) against and for all liability, costs, expenses, claims and damages which (ARCO) may at any time suffer or sustain or become liable for by reason of any accidents, damages or injuries either to the persons, or property or both of (PPI), or of the workmen of either party, or of any other parties, or to the property of (ARCO) in any matter arising from the work performed hereunder, including but not limited to any negligent act or omission of (ARCO), its officers, agents or employees. ... (Emphasis added by author.)

The court held the language "any negligent act of ARCO" was sufficient to define the parties' intent.

(d) *Enserch*. In *Enserch Corp. v. Parker*, 794 S.W.2d 2 (Tex. 1990), the Texas Supreme Court held the indemnity provision set out below **met** the express negligence test and required Christie, Inc. to indemnify Enserch for Enserch's negligent supervision of Christie, Inc.'s work as an independent contractor hired to service Enserch's pipeline. Parker, an employee of Christie, Inc., was asphyxiated when a gasket blew out causing a valve to leak natural gas into the concrete manhole vault where Parker was working. Parker's estate brought a wrongful death action against Enserch.

The court first held that Enserch owed a duty of care to the employees of Christie, Inc., even though Christie, Inc. was an independent contractor, since Enserch had retained control of the manner that Christie, Inc. was to carry out its servicing contract. Enserch had furnished a procedures book for Christie's employees which outlined the procedures to be followed while working on the pipeline, and Enserch representatives frequently visited the job site and supervised Christie's employees. The supreme court followed the exception announced in *Redinger v. Living, Inc.*, 689 S.W.2d 415, 418 (Tex. 1985) to the general rule of *Abalos v. Oil Dev. Co.*, 544 S.W.2d 627, 631 (Tex. 1976). The general rule adopted in *Abalos* is that an owner or occupier of land does not have a duty to see that an independent contractor performs work in a safe manner. However, the court in *Redinger* created an exception by holding that "one who entrusts work to an independent contractor, but who retains the control of any part of the work, is subject to liability for physical harm to others for whose safety the employer owes a duty to exercise reasonable care, which is caused by his failure to exercise his control with reasonable care." *Id.* at 418 [citing RESTATEMENT (SECOND) OF TORTS § 414 (1977)].

The court **upheld** the following provision as requiring Christie, Inc. to indemnify Enserch for Enserch's negligent supervision:

Provision:

> (Christie) assumes entire responsibility and liability for any claim or actions based on or arising out of injuries, including death, to persons or damages to or destruction of property, sustained or alleged to have been sustained in connection with or to have arisen out of or incidental to the performance of this contract by (Christie), its agents and employees, and its subcontractors, their agents and employees, regardless of whether such claims or actions are founded in whole or in part upon alleged negligence of (Enserch), (Enserch's) representative, or the employees, agents, invitees, or licensees thereof. (Christie) further agrees to indemnify and hold harmless (Enserch) and its representatives, and the employees, agents, invitees and licensee thereof in respect of any such matters and agrees to defend any claim or suit or action brought against (Enserch), (Enserch's) representative, and employees, agents, invitees, and licensees thereof... . (Court's emphasis.)

The court found that it was clear that "any such matters" in the second sentence referred to the claims or actions described in the first sentence and the contract as a whole was sufficient to define the parties' intent that Christie indemnify Enserch for the consequences of Enserch's own negligence. Therefore, the indemnity language and the reference to Enserch's negligence did not need to be in the same sentence.

(e) *Maxus*. The Texas Supreme Court in *Maxus Exploration Co. v. Moran Bros., Inc.*, 773 S.W.2d 358 (Tex. App.--Dallas 1989), *aff'd* 817 S.W.2d 50, 56 (Tex. 1991) **approved** the following language as meeting the express negligence test:

Provision:

> **14.9 Operator's Indemnification of Contractor:** Operator (Diamond Shamrock n/k/a Maxus) agrees to ... indemnify ... Contractor (Moran Bros.) ... from and against all claims ... of every kind ... without limit and without regard to the cause or causes thereof or the negligence of any party or parties, arising in connection herewith in favor of Operator's employees or Operator's contractors or their employees... on account of bodily injury, death or damage to property. ...
>
> **14.13 Indemnity Obligation:** Except as otherwise expressly limited herein, it is the intent of the parties hereto that all indemnity obligations and/or liabilities assumed by such parties under the terms of this Contract, including without limitation, paragraphs 14.1 ... be without limit and without regard to the cause or causes thereof ... strict liability, or the negligence of any party, whether such negligence be sole, joint or concurrent, active or passive. (Underlining added.)

The *Maxus* case is discussed below concerning the advisability of having a choice of laws provision in an indemnity agreement. The oil well drilling contract in *Maxus* failed to contain a choice of laws provision.

Diamond Shamrock (n/k/a Maxus), the operator, defended Moran Bros., the contractor, against a claim filed in a Kansas court by Boydstun, an employee of a contractor of Diamond Shamrock, against Moran. The Kansas jury found that Moran Bros. was 90% liable and awarded a $3,000,000 verdict, which was thereupon reduced to $2,700,000. Diamond Shamrock then sued in Texas for a declaratory judgment to declare the indemnity invalid. In applying the balancing test set forth in the RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6 (1971), the Texas Supreme Court held that Kansas law applied and under the "clear and unequivocal language" applicable to indemnities in Kansas, the indemnity was enforceable. However, the court additionally found that the indemnity provisions conformed to the public policy of Texas contained in the express negligence test.

The indemnity provisions in *Maxus* are from the standard form Daywork Drilling Contract published by the International Association of Drilling Contractors.

(f) *Fisk Electric*. The Texas Supreme Court in *Fisk Elec. Co. v. Constructors & Assoc., Inc.*, 888 S.W.2d 813 (Tex. 1994) found that the following language **did not** meet the express negligence test:

Provision:

> ...[t]o the fullest extent permitted by law, [Fisk] shall indemnify, hold harmless and defend [Constructors] ... from and against all claims, damages, losses, and expenses, including but not limited to attorney's fees [arising out of or resulting from the performance of Fisk's work].

Constructors brought a third party cause of action against Fisk seeking indemnification against the claim of Fisk's employee against Constructors. The court held that Fisk had no duty to indemnify Constructors, since the indemnity did not expressly cover Fisk indemnifying Constructors for Constructors' negligence. The court then found that since Fisk had no duty to indemnify Constructors, Fisk had no liability for Constructors' attorneys fees in defending against Fisk's employee's suit. *Id.* at 815.

(g) *Gulf Insurance Co.* The Texas Supreme Court in *The Gulf Ins. Co. v. Burns Motors*, 22 S.W.3d 417 (Tex. 2000) found that the express negligence test was not applicable in a case where the Indemnified Person was seeking indemnity for the consequence of the Indemnifying Person's act. The act of the Indemnified Person fell in the court's judgment clearly within the exclusion from indemnity. In *Gulf Ins.* suit was brought by the plaintiff (Burns Motors) in an earlier suit that had obtained an agreed judgment against Gulf's insurance agent (Nash). The court held that under the terms of agreed judgment the insurance agent acknowledged that he had knowingly passed on false information as to the coverage of the policy to his customer. Burns Motors took an assignment of the agent's claim of indemnity against the insurance company as set out in the Agency-Company Agreement executed by the agent and the company. The court found that the knowing misrepresentation of the policy's coverage by the agent fell within the exclusion

to indemnification contained in the following provision in the agency agreement.

Provision:

> Company (Gulf Insurance) will indemnify and hold harmless Agent against any claims or liabilities Agent may become obligated to pay to or in behalf of any insured based on actual or alleged error of Company in its processing or handling Direct Billed or any other business placed by Agent with Company, *except to the extent Agent has caused, contributed to or compounded such error.*

The court noted that although the parties argued extensively as to the application of the express negligence test to the indemnity provision, the express negligence test does not apply in a case where it is the acts or omissions of the Indemnifying Person that are sought to be recovered on as opposed to a case where one is seeking to be indemnified against one's own negligence. Here, the act of the Indemnified Person fell within the contractual exclusion from the indemnity.

(2) Court of Appeals Applications of *Ethyl*.

(a) Beaumont Court of Appeals. The Beaumont Court of Appeals, in *Faulk Management Services v. Lufkin Industries, Inc.,* 905 S.W.2d 476 (Tex. App.--Beaumont 1995, *writ denied*), upheld the following provision as covering injuries to an employer's employees caused by the sole negligence of the Indemnified Person (premises owner) even though injuries to the contractor/employer's employees was not specifically mentioned, and the indemnity provision was worded in terms of injuries "caused by the (contractor/employer)" and did not expressly mention that it covered injuries "caused by" the Indemnified Person

Provision:

> By signing the below statement, the seller (meaning Faulk Management as the "seller" of janitorial services) agrees to ... indemnify ... Lufkin Industries, Inc. against loss ... caused by the seller, its employees, agents or any subcontractor arising out of or in consequence of the performance of this contract.
>
> It is the intention of the Seller and/or Contractor to indemnify Lufkin Industries, Inc. even in the event that any such claims, demands, actions or liability arises *in whole* or in part from warranties, express or implied, defects in materials, workmanship or design, condition of property or its premises and/or *negligence* of Lufkin Industries, Inc. or any other fault claims as a basis of liability for Lufkin Industries, Inc.

(b) Corpus Christi Court of Appeals.

i) *ARCO v. McGuffin*. *Atlantic Richfield Oil & Gas Co. v. McGuffin*, 773 S.W.2d 711 (Tex. App.-- Corpus Christi 1989, *writ dism'd*). *McGuffin* is an earlier court of appeals' decision upholding the language from the Daywork Drilling Contract later approved by the Texas Supreme Court in *Maxus*. In *McGuffin*, ARCO sought indemnity for the $300,000 portion of a $1,000,000 agreed judgment in the wrongful death action brought by the estate of the contractor's deceased employee as was covered by the insurance requirement imposed by the contract on the contractor. The contract required the contractor to maintain the following insurance:

Provision:

> 8.1 Without limiting the indemnity obligations or liabilities of Contractor or its insurers, at any and all times during the term of this agreement, Contractor agrees to carry insurance of the types and in minimum amounts as follows:
> ...
> c. Comprehensive General Liability Insurance; including contractual liability insuring the indemnity agreement as set down in the agreement with minimum limits of $300,000 applicable to bodily injury, sickness or death in any one occurrence. ...

Id. at 714. The court **upheld** the contractor's agreement to indemnify the owner and found that the indemnity language expressly covered the owner's negligence. The court found that the insurance requirement did not exceed the limits imposed on indemnity insurance contained in TEX. CIV. PRAC. & REM. CODE ANN. § 127.005 (Vernon 1997) in what is known as the Texas Oilfield Anti-Indemnity Statute. The insurance did not exceed the limit so-imposed of 12 times the State's basic limits for personal injury as approved by the State Board of Insurance (12 x $25,000). [Higher limits are now permitted; *see* § 127.005 (Vernon 1997).] Therefore, the contractor's indemnity was within the exception permitted by the Oilfield Anti-Indemnity Statute prohibiting indemnities in oil and gas contracts except when the indemnity is supported by liability insurance up to the permitted amount. The court found that the indemnity was enforceable up to the permitted level of insurance.

ii) *Getty Oil Corp. v. Duncan: Round 1*. The Corpus Christi Court of Appeals in *Getty Oil Corp. v. Duncan*, 721 S.W.2d 475 (Tex. App.--Corpus Christi 1986, *writ ref'd n.r.e.*) held the following provision meant what it said, that the indemnified person was **not** being indemnified for its own negligence, in a case where the jury found the indemnified person (Getty) was 100% negligent

Provision:

> Seller (NL Industries-the chemical supplier) shall indemnify ... Purchaser (Getty) ... from any and all losses .... Seller shall not be held responsible for any losses ... caused by the negligence of Purchaser.

This provision is not quoted in the 1986 opinion (Round 1) but is set forth in the 1991 opinion (Round 2) discussed below in the portion of this Article concerning Coordinating Insurance With Indemnity Provisions.

(c) Dallas Court of Appeals. *Adams v. Spring Valley Const. Co.*, 728 S.W.2d 412 (Tex. App.--Dallas 1987, *writ ref'd n.r.e.*). This case

involved construction of an indemnity provision in a subcontract between the general contractor and the subcontractor and in a certificate of insurance. The court held that the contract provisions, even when taken together with the insurance certificate, **did not meet** the express negligence standard. Both documents contained a provision whereby the subcontractor would indemnify the contractor for all liability arising from or out of the contractor's work on the project. The insurance certificate contained an indemnity as to liabilities "caused in whole or in part by a negligent act of the Subcontractor ... regardless of whether it is caused in part by a party, indemnified hereunder." The court found that the indemnity provision did not cover liabilities in the event that the contractor was 100% negligent.

The Dallas court in *Arthur's Garage v. Racal-Chubb*, 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*)[an alarm security products liability case where the tenant indemnified the alarm company from claims by third parties, which included the claim of the landlord] found that the following provision clearly and specifically **covered** the Indemnified Person's negligence, breach of warranty, and strict product liability:

Provision:

> When purchaser (Arthur's Garage), in the ordinary court of business, has the property of others in his custody, or the alarm system extends to protect the property of others, purchaser agrees to and shall indemnify, defend, and hold harmless seller, its employees and agents for and against all claims brought by parties other than the parties to this agreement. This provision shall apply to all claims, regardless of cause, including seller's performance or failure to perform, and including defects in products, design, installation, maintenance, operation or non-operation of the system, whether based upon negligence, active or passive, warranty, or strict product liability on the part of seller, its employees or agents, but this provision shall not apply to claims for loss or damage solely and directly caused by an employee of seller while on purchaser's premises.

This case is also discussed below in connection with the enforceability of contractual limitations of liability.

(d) Eastland Court of Appeals. In *Banzhaf v. ADT Sec. Sys.*, 28 S.W.3d 180 (Tex.App.-Eastland [11th Dist.] 2000, *writ denied*) the court of appeals **upheld** the following indemnity provision in an alarm security services contract. The court rejected Herman's argument that the identification of claims arising out of ADT's negligence as being covered by the indemnity had to be in the same sentence with the word "*indemnify*." ADT obtained indemnity against its customer, Herman Sporting Goods, Inc., for claims made by the estate of a Herman's employee who was killed in a robbery. The alarm service purchased by Herman's was fire alarm and after-hours unauthorized entry detection services and not robbery or hostage detection services. The alarm service purchased by Herman's was designed to go on only when no employees were in the store. Herman's had declined to add the "duress code" feature to the alarm. The decedent employee's estate argued that ADT's project was defective in not having this feature as a mandatory service.

Provision:

> In the event any person, not a party to this agreement, shall make any claim or file any lawsuit against ADT for failure of its equipment or service in any respect, customer [Herman's] agrees to indemnify, defend, and hold ADT harmless from any and all such claims, and hold ADT harmless from any and all such claims and lawsuits including the payment of all damages, expenses, costs, and attorney's fees. The customer [Herman's] ... agrees that ADT shall be exempt from liability for loss, damage or injury due directly or indirectly to occurrences, or consequences therefrom, which the service or system is designed to detect or avert; that if ADT should be found liable for loss, damage or injury due to a failure of service or equipment in any respect, its liability shall be limited to a sum equal to 100% of the annual service charge or $10,000, whichever is less ... as the exclusive remedy; and that the provisions of this paragraph shall apply if loss, damage, or injury, irrespective of cause or origin, results directly or indirectly to person or property from performance or nonperformance of obligations imposed by this contract or from *negligence*, active or otherwise, of ADT, its agents or employees. (emphasis added)

(e) El Paso Court of Appeals. *Permian Corp. v. Union Texas Petroleum Corp.*, 770 S.W.2d 928 (Tex. App.--El Paso 1989, *no writ*). An employee of a subsidiary of Permian, the contractor, sued Union Texas for negligently causing the employee injuries while the employee was performing services for Union Texas. The El Paso Court of Appeals found the following indemnity by Permian **expressly indemnified** Union Texas against liabilities arising out of its negligence:

Provision:

> Contractor (Permian) hereby indemnifies and agrees to protect, hold and save Union Texas ... harmless from and against all claims ... including but not limited to injuries to employees of Contractor ... on account of, arising from or resulting, directly or indirectly, from the work and/or services performed by Contractor ... and whether the same is caused or contributed to by the negligence of Union Texas, its agents or employees. (Emphasis added by the court.)

"Whether" was interpreted to mean "including, even if ... ."

(f) Fort Worth Court of Appeals.

i) *Linden-Alimak*. *Linden-Alimak, Inc. v. McDonald*, 745 S.W.2d 82 (Tex. App.--Ft. Worth 1988, *writ denied*). The Fort Worth Court of Appeals reviewed an indemnity provision in an equipment rental agreement. An employee (McDonald) of the equipment lessee (Thomas S. Byrne, Inc.) filed suit against the equipment lessor (Linden-Alimak) to recover damages for personal injuries sustained while

the leased crane was being erected. The equipment lessor filed a third party action against the lessee for indemnification. The court held that the following indemnity provision in the equipment lease agreement suffered the same defect as the provision in *Crown Central Petroleum.* The court found the indemnity language to be **inadequate** to indemnify the equipment lessor against its concurrent negligence. The indemnity, by excluding the lessor's sole negligence, did not include a case of lessor's concurrent negligence. Situations involving lessor's concurrent negligence were not mentioned (*i.e.*, "in part" not mentioned).

Provision:

> It is expressly understood and agreed that Lessor shall not be liable for damages, losses and injuries of any kind whatsoever, whether to persons or property, or for any other loss arising from the operation, handling, use of, transportation of, or in any way connected with the said equipment or any part thereof from whatsoever cause arising, except direct damages, losses or injuries caused by Lessor's sole negligence. Lessee shall indemnify and save Lessor harmless from any and all claims, demands, liabilities, judgments, actions or causes of action of any nature whatsoever (except if caused by Lessor's sole negligence) arising out of the selection, possession, leasing, operation, control, use, maintenance, repair, adjustment or return of the equipment. (Emphasis added by author.)

ii) *B-F-W Construction*. In *B-F-W Const. Co., Inc. v. Garza*, 748 S.W.2d 611 (Tex. App.--Ft. Worth 1988, *no writ*), the Fort Worth Court of Appeals held that the language "regardless of any cause or of any fault or negligence of Contractor" **expressly stated** the intent of the parties that the subcontractor would indemnify the contractor against the contractor's negligence. The indemnity provision stated

Provision:

> Subcontractor (Garza Concrete) shall fully protect, indemnify and defend contractor (B-F-W) and hold it harmless from and against any and all claims, demands, causes of action, damages and liabilities for injury to or death of Subcontractor, or any one or more of Subcontractor's employees or agents, or any subcontractor or supplier of Subcontractor, or any employee or agent of any such subcontractor or supplier, arising in any manner, directly or indirectly, out of or in connection with or in the course of or incidental to any work or operations of Subcontractor or Contractor or any other contractor or subcontractor or party, or otherwise in the course and scope of their employment, and regardless of cause or of any fault or negligence of Contractor. (Emphasis added by author.)

(g) Houston Courts of Appeals.

i) 1st District. *Monsanto Co. v. Owens-Corning Fiberglass Corp.*, 764 S.W.2d 293 (Tex. App.--Houston [1st Dist.] 1988, *no writ*). The employee of the subcontractor (Owens-Corning) sued the contractor (Monsanto) for personal injuries suffered on the job site. The employee had already collected workers' compensation benefits from the subcontractor. The contractor filed a third party action against its subcontractor seeking contractual indemnity. The court held the following provision in the subcontract **did not meet** the express negligence standard since it did not expressly indemnify the contractor for its own negligence:

Provision:

> (Sub)Contractor (Owens-Corning) agrees to indemnify and save Monsanto (Contractor) and its employees harmless against any and all liabilities, penalties, demands, claims, causes of action, suits, losses, damages, costs and expenses (including costs of defense, settlement and reasonable attorney's fees) which any or all of them may hereafter suffer, incur, be responsible for or pay out ... as a result of bodily injuries ... to any person or damage ... to any property occurring to or caused in whole or in part by, (Subcontractor) (or any of his employees), any of his (Sub)Subcontractors (or any employee thereof) directly or indirectly employed or engaged by either (Subcontractor) or any of his (Sub-subcontractors). (Emphasis and parenthetical designations added by author.)

The court noted that the term "negligence" is not found in the indemnity agreement. The indemnity did not mention indemnifying against the negligence of the contractor. Also, it did not mention indemnifying against the concurrent negligence of the subcontractor (the indemnifying party). Therefore, the court noted that the agreement **did not provide for contractual comparative negligence**. The indemnity contract neither covered the negligence of the contractor nor the subcontractor. *Id.* at 295. The indemnity also does not expressly require the employer (Indemnifying Person) to assume liability for injuries to its employees thereby overcoming the Workers' Compensation Bar.

The court in *Jobs Building Services, Inc. v. Rom, Inc.*, 846 S.W.2d 867 (Tex. App.--Houston [1st Dist.] 1992, *writ denied*) found that the following provision in a window washing subcontract with the building maintenance contractor was **not** specific enough to indemnify the contractor for its own negligence:

Provision:

> The Subcontractor agrees to indemnify and hold harmless the Contractor ... for (i) bodily injury, illness or death of any person; ... which ... damage is caused by the Subcontractor's negligent act or omission or by the negligent act or omission of anyone employed by the Subcontractor or for whose acts the **Contractor** or the Subcontractor **may be liable** or for which the Subcontractor is liable or responsible. (Court's italics; author's bold.)

Id. at 870.

Glendale Construction Services, Inc. v. Accurate Air Systems, Inc., 902 S.W.2d 536 (Tex. App.–Houston [1st Dist.] 1995, *writ denied*). The court, following the Texas Supreme Court's ruling in *Fisk Electric Co. v. Constructors, Inc.,* 888 S.W.2d 813 (Tex. 1994) construing a similar provision, held the following provision did **not** pass the express negligence test.

Provision:

> 11.11 Indemnification:
>
> To the fullest extent permitted by law, the Subcontractor shall indemnify and hold harmless the Owner, the Architect and the Contractor and all of their agents and employees from and against all claims, damages, losses and expenses, including but not limited to attorney's fees, *arising out of or resulting from the performance of the Subcontractor's work under this Subcontract* provided that any such claim ... *to the extent caused in whole or in part by a negligent act or omission of the Subcontractor or anyone directly or indirectly employed by him or anyone whose acts he may be liable, regardless of whether it is caused in part by a party indemnified hereunder. ...*

The language referring to the Indemnified Person only referred to injuries "whether caused in part" by the Indemnified Person, and did not expressly state that the cause was the "negligence" of the Indemnified Person. This type of indemnity provision is the same as is contained in the AIA forms. *See* **Appendix 3**. The court also noted that the next provision in the indemnity, the standard waiver of the workers' compensation bar (the "indemnification obligation ... shall not be limited in any way by any limitation on the amount or type of damages, compensation or benefits payable by or for the Subcontractor under workers' or workmen's compensation acts...") was irrelevant since the indemnity was not otherwise enforceable.

ii) 14th District. The court in *Adams Resources Exploration Corp. v. Resource Drilling, Inc.*, 761 S.W.2d 63 (Tex. App.--Houston [14th Dist.] 1988, *writ dism'd*) found the indemnity provision **passed** the express negligence test. The indemnity language in this case is identical to the language recently reviewed by the Texas Supreme Court in *Maxus Exploration Co. v. Moran Bros., Inc.*, 773 S.W.2d 358 (Tex. App.--Dallas 1989), *aff'd* 817 S.W.2d 50 (Tex. 1991) discussed above and is contained in the standard form Daywork Drilling Contract published by the International Association of Drilling Contractors.

In *DDD Energy, Inc. v. Veritas DGC Land, Inc.*, 60 S.W.3d 880 (Tex.App.-Houston [14th Dist.] 2001, *no writ*), the court of appeals found that the following provision **was not** enforceable to shift DDD's negligence to Veritas, but did not prevent DDD from recovery from Veritas on a claim that Veritas breached its contract to perform its services in a good and workmanlike manner:

Provision:

> Section V-Operations:
>
> Veritas shall **indemnify**, defend, ... [DDD] for all claims, damages, causes of actions, and liabilities resulting from **Veritas' failure to conduct seismic operations in an orderly and workmanlike manner**...
>
> Section X-Liability Indemnity:
>
> Veritas shall protect, **indemnify**, defend and save [DDD], ... harmless from and against all claims, ... and causes of action ... asserted by third parties on account of ... damage to property of such third parties, which ... damage is the result of the **negligent act or omission**, breach of this Basic Agreement or the Supplemental Agreement, or willful misconduct **of Veritas** ... Likewise, [DDD] shall protect, indemnify, defend and save Veritas, ... harmless from and against all claims, ... causes of action ... asserted by third parties on account of ... damage to property of such third parties, which ... damage is the result of the negligent act or omission or willful misconduct of [DDD] ...

Suit was brought by Vickers, a landowner, against DDD, which was the lessee on an oil and gas lease covering Vickers' land, for property damages sustained by Vickers due to the cutting down of numerous oak and mesquite trees. DDD had hired Veritas to conduct seismic services on the Vickers' land. Veritas subcontracted with Brush Cutters to conduct brush clearing operations. DDD brought suit against Veritas seeking a declaratory judgment that Veritas is obligated to defend and indemnify DDD against claims based on damage to Vickers' land caused by Veritas' negligence.

The court of appeals sustained the trial court's granting of summary judgment against enforcement of the indemnity provision. The court of appeals found that DDD's action was an attempt to have Veritas indemnify DDD for DDD's negligence.

However, the court reversed the trial court and remanded the matter for further proceedings regarding Veritas' obligations under the indemnity provisions to defend and indemnify DDD against third party claims not based on DDD's negligence. Vickers had sued DDD for (1) breach of duty to manage and administer the lease, (2) breach of contract, (3) negligence, (4) malicious trespass, (5) negligent misrepresentations, (6) breach of fiduciary duty, (7) gross negligence, and (8) intentional tort.

(h) San Antonio Court of Appeals. *Haring v. Bay Rock Corp.*, 773 S.W.2d 676 (Tex. App.--San Antonio 1989, *no writ*). In this case involving a wrongful death action, the San Antonio Court of Appeals held the following provision **did not meet** the express negligence test since the negligence of the alleged indemnified person (oil and gas lessee) is not mentioned:

Provision:

> [Operator (Bay Rock Corp.)] shall have no liability to owners of interests in said wells and leases (Haring) for losses sustained, or liabilities incurred, except such as may result from gross negligence or from breach of the provisions of this agreement.

The provision is worded as a disclaimer by the operator as to any liability except for gross negligence, and not as an indemnification by the operator for the operator's "disclaimed" but not expressly disclaimed negligence.

(i) Texarkana Court of Appeals. The Texarkana Court of Appeals in *Texas Utilities*

Electric Co. v. Babcock & Wilcox, 893 S.W.2d 739 (Tex. App.--Texarkana 1995, *no writ*) found that **neither** of the following indemnity provisions expressly covered the Indemnified Person's (Texas Utilities') concurrent negligence in causing injuries to an employee of Flour Daniel, a contractor employed by Texas Utilities.

Provisions:

> [Babcock & Wilcox agree to indemnify Texas Utilities for claims against Texas Utilities for damages arising from] personal injury or death or damage to property of Company's [Babcock's] agents, servants and employees, as well as the agents, servants, and employees of Company's [Babcock's] subcontractor, whether or not arising from sole or concurrent negligence or fault of Purchaser [TU].
>
> [Babcock & Wilcox] shall defend ... indemnify ... Purchaser [TU] and its ... agents ... from and against any and all claims ... of every kind and character whatsoever arising in favor of any person or entity (other than the agents, servants, and employees or [*sic]* [of?] Company [Babcock] or of Company's subcontractor, as provided in the paragraph immediately above), including ... claims ... on account of personal injuries or death, or damage to property arising out of or incident to the work performed hereunder .... with the only exception being that, as to claims arising in favor of persons or entities other than for injury, death, or damage to the agents, servants, and employees of Company [Babcock] or Company's subcontractor, Purchaser [TU] shall not be entitled to indemnification for claims, demands, expenses, judgments, and causes of action resulting from Purchaser's [TU] sole negligence.

The first indemnity does not cover injuries to employees of a contractor of Texas Utilities. The second indemnity does not cover Texas Utilities' concurrent negligence. The exception for Texas Utilities' sole negligence from the broad indemnity is not equivalent to an express inclusion of Texas Utilities' concurrent negligence.

(j) Tyler Court of Appeals. In *State Department of Highways & Public Transportation v. Reynolds-Land, Inc.*, 757 S.W.2d 868, 869 (Tex. App.--Tyler 1988, *no writ*), the Tyler Court of Appeals held **unenforceable** the following indemnity provision in a highway construction contract between the State Highway Department and the contractor:

Provision:

> The contractor (Reynolds-Land) shall save harmless the (Department) from all account of any injuries or damages sustained by any person or property in consequence of any neglect in safeguarding the work by ... (Reynolds-Land); or from any claims or amounts arising or recovered under the "Workmen's' Compensation Laws" or any other laws.

The amounts for which indemnity was sought were paid by the Department pursuant to an agreed judgment setting a negligence suit brought by the injured employee of the contractor against the Department. The contractor's workers' compensation carrier had intervened in the suit to seek subrogation against the Department for amounts it had paid to the employee. Unfortunately for the Department, the court held that the settlement amounts paid by the Department were in the nature of settlement payments on the claim against the Department for its own negligence, rather than amounts paid by it on a workers' compensation claim. The indemnity clause neither expressly covered the Department's negligence nor amounts paid by the Department to settle claims against the Department for its own negligence. Also, even though the indemnity clause expressly covers "any claims over amounts arising or recovered under the Workmen's Compensation Laws," the Department could only be liable at common law for its own negligence; and therefore, the settlement agreement could not transform the payment from a payment on account of the Department's negligence to a claim paid by it under the Workers' Compensation Act.

(3) Federal Court Interpretations of *Ethyl*.

(a) *Dupont v. TXO Production*. *Dupont v. TXO Production Corp.*, 663 F. Supp. 56 (E.D.Tex. 1987). The Eastern District Court **enforced** an indemnity provision where a contractor (Richards) indemnified the owner of a rig (TXO) for injuries incurred by contractor's employees "without regard to the cause or causes thereof or the negligence of any party ... ." This language is identical to the language approved by the Texas Supreme Court in *Maxus Exploration Co. v. Moran Bros., Inc.*, 773 S.W.2d 358 (Tex. App.--Dallas 1989), *aff'd* 817 S.W.2d 50 (Tex. 1991).

(b) *Hardy v. Gulf Oil*. In *Hardy v. Gulf Oil Corp.*, 949 F.2d 826 (5th Cir. 1992), the court, after exhaustively examining Texas statutory and common law and general maritime law, easily disposed of the offshore oil well contractor's claim for indemnity since, unfortunately, the Drilling Contract did **not** contain an indemnity provision. *See generally* Yeates, Dye & Garcia, *Contribution and Indemnity in Maritime Litigation*, 30 S. TEX. L. REV. 215 (1989).

(c) *Barnes v. Calgon Corp*. The court in *Barnes v. Calgon Corp.*, 872 F. Supp. 349 (E.D. Tex. 1994) did not find it even necessary to discuss the express negligence test in **upholding** the following provision as covering the negligence of the Indemnified Person (Calgon who had loaned its employee to Pacemaker Employee Leasing, Inc.):

Provision:

> Southwestern Professional Driver Service (Pacemaker) will indemnify ... from any claims ... of its employees (Barnes who was a borrowed servant/employee from Calgon) ... including: Payroll ... injury ... regardless of whether such claims are alleged to have been caused in whole or in part of any act of negligence of Calgon ....

C. Indemnity Against One's Strict Liability. The fair notice doctrine has been extended to cases involving strict liability. The Texas Supreme Court

held in *Houston Lighting & Power Co. v. Atchison, Topeka, & Santa Fe Railway Co.,* 890 S.W.2d 455 (Tex. 1994) that an indemnity agreement will include indemnification for strict statutory liability only if the agreement expressly states that the Indemnifying Person is to be liable for the Indemnified Person's strict liability. In *Houston, Lighting & Power*, the court held that the provision outlined below did not indemnify Railway Company for the strict liability imposed by the Federal Employers' Liability Act (FELA) for injuries to its employee. 45 U.S.C.A. §§ 51-60 (1988).

Provision:

> Notwithstanding anything contained in Section 3 of Article 1 of Original Contract to the contrary, [HL&P] agrees that it will at all time indemnify and save harmless Railway Company against all claims, demands, actions or causes of action, arising or growing out of loss of or damage to property, including said rotary dumper and appurtenances, and injury to or death of persons, including employees of Railway Company, resulting in any manner from the construction, maintenance, use, state of repair or presence of said rotary dumper and appurtenances under of adjacent to The Track, *whether such loss, damage, injury or death be caused or contributed to by the negligence of Railway Company, its agents or employees, or otherwise* ....

An employee of the Railway Company sued it for injuries the employee sustained in uncoupling a railroad coal car at a coal dumping facility at HL&P's power plant. HL&P operated a rotary coal dumper at its plant. A rotary coal dumper unloads a coal train by moving each car into position inside the dumper through the use of a mechanical arm. Rotary couplers link the coal cars together and allow the dumper to invert the coal car and empty the coal into an underground pit. Because the caboose does not have a rotary coupler, the last car must be uncoupled from the caboose before being emptied. After the employee had successfully unloaded the cars of coal, he attempted to realign the couplers on the caboose, which had failed to realign. The employee injured his back in the process. The Federal Safety Appliance Acts (SAA), 45 U.S.C.A. § 2 (1988) mandate that couplers on the cars and the caboose remain aligned so that they will automatically couple upon impact with the preceding or following car without the necessity of workmen having to go between the cars. FELA embraces claims of an employee based on a violation of the SAA.

HL&P entered into the above indemnity agreement indemnifying the Railway Company as to liability for injuries to the Railway Company's employees. The jury found that the employee was 45% negligent and that the Railway Company was 55% negligent.

The supreme court determined, however, that the indemnity provision did not cover this type of liability. The court found that the Railway's strict liability for injuries to its employees arising out of a violation of the SAA was not a negligence-based liability, but a strict statutory liability. The Railway Company argued that its liability for a SAA violation was negligence *per se*, and therefore "negligence" within the words of the indemnity provision.

However, the supreme court determined that the correct view of the liability created by the SAA was that it was a strict liability not dependent upon the negligence of the Railway Company. It noted that confusion and contrary decisions had arisen in this area, in part, because a claim based on a violation of the SAA is a non- negligence claim, which must be pursued by action under FELA, a negligence-based statute. The court overruled its earlier decision in *Missouri-Kansas-Texas R.R. v. Evans,* 250 S.W.2d 385, 392 (Tex. 1952) in which the court had held "in passing" that a violation of the SAA is negligence *per se*.

The court found that fairness dictates that such an "**extraordinary shifting of risk**" must be clearly and specifically expressed as to non-negligence based statutory strict liability in order to be enforced.

The court in passing recognized that indemnity provisions shifting liability arising out of **strict products liability** are similarly enforceable, if fair notice has been given. *Citing Rourke v. Garza,* 511 S.W.2d 331, 333 (Tex. Civ. App.--Houston [1st Dist.] 1974), *aff'd*, 530 S.W.2d 794 (Tex. 1975)--in which the indemnity clause was held not to have been worded sufficiently so as to include strict products liability; *Dorchester Gas Corp. v. American Petrofina, Inc.* 710 S.W.2d 541, 543 (Tex. 1986)--also, which held that the indemnity clause in question did not clearly require the indemnitor to indemnify the indemnitee against strict products liability. *See* Richard L. Scheer, *Model Contractual Indemnity Provisions Effective to Protect an Indemnitee Against His Own Negligence or Other Fault,* 50 TEX. B.J. 602, 606 (June 1987). *See* Tade, *Indemnification - Who Wins, Who Loses Under Texas, Louisiana and Maritime Law,* 29TH ANNUAL OIL, GAS & MINERAL LAW INSTITUTE 10 (UNIV. TEX. 1994) *citing Armstrong v. Chambers & Kennedy,* 340 F. Supp. 1220 (S.D. Tex. 1972); *aff'd and rev'd in part on other grounds sub nom., In re Dearborn Marine Services, Inc.,* 499 F.2d 263 (5th Cir. 1974), *cert. dismissed,* 423 U.S. 886 (1974); *Dorchester Gas Corp. v. American Petrofina, Inc.,* 710 S.W.2d 541 (Tex. 1986), *overruled by Ethyl*; *K&S Oil Well Service, Inc. v. Cabot Corp.,* 491 S.W.2d 733 (Tex. Civ. App.--Corpus Christi 1973, *writ ref'd n.r.e.*).

The Fifth Circuit has addressed indemnifications for strict liability under environmental protection laws in *Fina, Inc. v. ARCO*, 200 F.3D 266 (5th Cir. 2000). In *Fina* the court had to determine the enforceability of two indemnity provisions, the first in a 1969 sales contract between ARCO and BP Oil Company (the *"ARCO/BP Agreement"*) as to a refinery located in Port Arthur, Texas being acquired by BP from ARCO, and the second in a 1973 sales contract between BP and Fina (the *"BP/Fina Agreement"*) whereby Fina acquired the refinery from BP. Fina sued BP and ARCO for $14,000,000 in investigatory and remedial response costs it incurred after it discovered contamination at the refinery in 1989. Fina sought contribution from BP and ARCO under CERCLA. BP counterclaimed that the liability was covered in Fina's indemnity of BP in the BP/Fina Agreement. ARCO counterclaimed that the liability was covered by the

indemnity in the ARCO/BP Agreement was assumed by Fina by the BP/Fina Agreement. The BP/Fina Agreement contained an express choice of laws provision choosing Delaware law. The ARCO/BP Agreement was silent as to applicable law. The indemnity provisions are the following:

Provisions:

> ARCO/BP Agreement. BP shall indemnify, defend, and hold harmless ARCO ... against all claims, actions, demands, losses or liabilities arising from the ownership or the operation of the Assets ... and accruing from and after Closing ... except to the extent that any such claim, action, demand, loss or liability shall arise from the gross negligence of ARCO.
>
> BP/Fina Agreement. Fina shall indemnify, defend and hold harmless BP ... against all claims, actions, demands, losses or liabilities arising from the use or the operation of the Assets ... and accruing from and after closing.

As to the BP/Fina Agreement the court first determined that it would uphold the parties choice of Delaware law as the court could not discern a fundamental public policy of the State of Texas that would be violated by applying the "clear and unequivocal" test applicable to the enforceability of indemnity provisions covering the Indemnified Person's negligence. The court then held that the "all claims" language in the BP/Fina Agreement clearly covered liabilities arising under CERCLA, even though CERCLA was not enacted until 1980. The court noted that unlike Texas no Delaware case had addressed the applicability of the clear and unequivocal test to claims based on strict liability. The court found that the same policy reasons that existed in Texas' extension of the express negligence doctrine to strict liability cases also existed in Delaware to extend the clear and unequivocal test to strict liability claims in interpreting indemnities.

The court rejected BP's argument that normal contract rules of interpretation should apply to interpreting the indemnity. BP argued that the clear and unequivocal test should not apply to indemnification for *prior* acts giving rise to *potential future* liability (with "past" and "future" being determined by reference to the time at which the indemnity provision was signed). The court rejected BP's argument that under Texas law the express negligence doctrine is inapplicable to indemnities for past conduct giving rise to potential future liability and therefore similarly the court should find that Delaware would not apply the clear and unequivocal test to potential future liability for past acts.

The court stated,

> Even as to Texas law, it is not at all clear that BP's conclusion is correct. The language used by the Texas courts is ambiguous: "Future negligence" might refer to *future negligent conduct*, but it also might refer to *future claims based on negligence*. True, the Texas rule does clearly distinguish between (1) indemnification for past conduct for which claims have already been filed at the time the indemnity provision is signed and (2) indemnification for future conduct for which claims could not possibly have been filed at the time the indemnity provision was signed. Still, no Texas case has addressed the applicability of the rule to the rare situation in which a party attempts to invoke the protection of an indemnity agreement against a claim filed *after* the indemnity was signed but arising from conduct that occurred *prior* to signing of the indemnity.

The court held that under Delaware law the indemnity in the BP/Fina Agreement did **not** clearly and unequivocally require Fina to indemnify BP for its strict liability under CERCLA that arose after the indemnity agreement (the *"future claim"*) for conduct prior to the indemnity agreement.

As to ARCO's "circuitous indemnity obligation" being enforceable against Fina, the court held that the ARCO/BP Agreement did **not** pass the fair notice test under Texas law and would not pick up strict liability claims for ARCO's future strict liability for its past conduct.

The court noted that Fina's claims under the Resource Conservation Recovery Act, 42 U.S.C. §§ 6901 *et seq.*, and § 361.344 of the Texas Solid Waste Disposal Act similarly would not be barred by the indemnity.

D. Elements. An indemnity contract involves the same basic elements as contracts generally.

1. Offer and Acceptance. A contract of indemnity requires an offer and acceptance.

a. Authority to Enter Indemnity Contract. In *Rourke v. Garza*, 511 S.W.2d 331, 334 (Tex. Civ. App.--Houston [1st Dist.] 1974), *aff'd* 530 S.W.2d 794 (Tex. 1975), the Texas Supreme Court refused to enforce an indemnification clause contained in a delivery receipt for leased equipment. The receipt was signed by an employee of the contractor who did not have actual or apparent authority to bind the contractor and the contractor did not have actual knowledge of the terms set forth in the receipt prior to signature.

b. Failure to Read No Excuse. It has been held that the failure of an owner to call the attention of the contractor to an indemnity provision in a construction contract did not excuse the contractor from the indemnity provision absent proof of fraud, overreaching or mutual mistake. *Gulf Oil Corp. v. Spence & Howe Constr. Co.*, 356 S.W.2d 382 (Tex. Civ. App.--Houston 1962, *writ ref'd n.r.e.*), *aff'd* 365 S.W.2d 631 (Tex. 1963).

c. Conspicuous. *See* Greer and Collier, *The Conspicuousness Requirement: Litigating and Drafting Contractual Indemnity Provisions in Texas After Dresser Industries, Inc. v. Page Petroleum, Inc.*, 35 SO. TEX. L.REV. 243 (1994) and the discussion below of the *Dresser* case in **Article IV--Exculpation and Limitations of Liability Provisions and Releases** reviewing the application of the "conspicuousness" requirement to exculpation provisions and releases. An indemnity provision indemnifying the Indemnified Person against his own negligence must be conspicuous

enough to give the Indemnifying Person "fair notice" of its existence. The concept of "fair notice" was introduced into Texas indemnity law by the Texas Supreme Court in *Spence & Howe Const. Co. v. Gulf Oil Corp.,* 365 S.W.2d 631, 634 (Tex. 1963). The fair notice principle focuses on the appearance and placement of the provision as opposed to its "content." The supreme court in *Spence* reasoned that

> [t]he obvious purpose of this rule is to prevent injustice. A contracting party should be upon *fair notice* that under his agreement and through no fault of his own, a large and ruinous award of damages may be assessed against him solely by reason of negligence attributable to the opposite contracting party.

Spence, at 634.

Goodyear Tire & Rubber Co. v. Jefferson Constr. Co., 565 S.W.2d 916, 919 (Tex. 1978) **upheld** a provision on reverse side of purchase order where frontside contained reference in large red print, partly in bold, incorporating provisions on reverse side; *Enserch Corp. v. Parker*, 794 S.W.2d 2, 8 (Tex. 1990) upheld an indemnity provision contained on front of one page contract in separate paragraph; *Dresser Industries v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993) **struck down** indemnity located on back of work order, in a series of uniformly numbered paragraphs, with no heading and with no contrasting type; *K & S Oil Well Service, Inc. v. Cabot Corp., Inc.*, 491 S.W.2d 733, 737-38 (Tex. Civ. App.--Corpus Christi 1973, *writ ref'd n.r.e.*) struck down indemnity hidden on reverse of contract in paragraph headed "warranty;" *Rourke v. Garza*, 511 S.W.2d 331, 334 (Tex. Civ. App.--Houston [1st Dist.] 1974), *aff'd* 530 S.W.2d 794 (Tex. 1975); *Safway Scaffold Co. of Houston, Inc. v. Safway Steel Products, Inc.*, 570 S.W.2d 225, 228 (Tex. Civ. App.--Houston [1st Dist.] 1978, *writ ref'd n.r.e.*); *Griffin Indus. v. Foodmaker, Inc.*, 22 S.W.3d 33 (Tex.App.-Houston [14th Dist.] 2000, *writ ref'd*)-indemnity not conspicuous if in same size and type as the balance of a 1 page document; *Douglas Cablevision v. SWEPCO*, 992 S.W.2d 503 (Tex.App.-Texarkana 1999, *writ denied*)-indemnity provision not conspicuous if in same size and type and without a separate heading identifying the paragraph was an indemnity in a 22 paragraph, 13 page document, also court not persuaded that the conspicuousness requirement applied only to **"forms."**

The Texas Supreme Court discussed the UCC § 1.201(10) conspicuousness requirement in the context of warranties in *Cate v. Dover Corp.,* 790 S.W.2d 559 (Tex. 1990). In *Cate*, the court found that limitations to the product's warranty were "buried" and were therefore not conspicuous enough to be enforced. The court reviewed an advertisement that exclaimed in blue, half-inch print, "YOU CAN TAKE ROTARY'S NEW 5-YEAR WARRANTY AND TEAR IT APART." Below this statement was bold black print touting how "**solid**" the warranty was, how it was superior to other companies' warranties, and how it did not hide the limitations of the warranty in "mumbo jumbo." *Cate* at 560. The court defined the "conspicuous" standard as follows:

> We hold that, to be enforceable, a written disclaimer of the implied warranty of merchantability made in connection with a sale of goods must be conspicuous to a reasonable person. We further hold that such a disclaimer contained in text undistinguished in typeface, size or color within a form purporting to grant a warranty is not conspicuous, and is unenforceable unless the buyer has actual knowledge of the disclaimer.

Cate at 562.

In *Dresser Industries, Inc. v. Page Petroleum, Inc.,* 853 S.W.2d 505 (Tex. 1993), the supreme court adopted the conspicuousness standard of § 1.201(10) of the Texas UCC, applicable to the sale of goods, and applied it to indemnities and releases in a case involving the sale of services. Section 1.201(10) of the Texas UCC provides

> A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it. A printed heading in capitals (as: A NON-NEGOTIABLE BILL OF LADING) is conspicuous. Language in the body of a form is "conspicuous" if its is in larger or other contrasting type or color. But in a telegram any term is "conspicuous."

TEX. BUS. COMM. CODE § 1.201(10) (Vernon 1994). *Also see Banzhaf v. ADT Sec. Sys.*, 28 S.W.3d 180 (Tex.App.-Eastland [11th Dist.] 2000, *writ ref'd*) finding an indemnity to be conspicuous that was set forth in "enlarged, all capital lettering. The lettering is dark, boldface type so that it contrasts with the lighter, smaller type of the remaining contractual paragraphs ... The indemnity provision ... is directly above the signature line. A reasonable person's attention is attracted to the indemnity provision when looking at the contract... The indemnity provision is on the back page (of a 1 page document), but the contract itself specifically directs the reader's attention to the paragraph in which is it contained. On the front of the contract, just above the signature line for Herman's is the directive: "**ATTENTION IS DIRECTED TO THE WARRANTY, LIMIT OF LIABILITY AND OTHER CONDITIONS ON REVERSE SIDE**." An indemnity provision was held **not** to meet the conspicuousness requirement in *U.S. Rentals, Inc. v. Mundy Service Corp.*, 901 S.W.2d 789 (Tex. App.--Houston [14th Dist.] 1995, *writ denied*) when it was buried on the back of a rental contract with all provisions printed in the same respective type and sizes, and the heading did not alert the reader that it created an indemnity obligation ("LIABILITY FOR DAMAGE TO EQUIPMENT, PERSONS AND PROPERTY"). In response to the claimant's argument that due to the sophistication of the indemnitor and his experience in the construction industry, he would have noticed the indemnity provision, the court stated

> Contrary to U.S. Rentals' fourth argument, we read *Fisk, Dresser*, and other relevant decisions to direct that the conspicuousness of an indemnity agreement be established by **objective factors** on the face of the agreement, rather than to vary according to the

subjective sophistication and experience of each party against whom the agreement may be asserted.

Id. at 792.

The Supreme Court in *Littlefield v. Schaefer*, 955 S.W.2d 272 (Tex.1997), found that a release was **not** conspicuous when it was set in a type font too small to read even though the heading was in larger font (heading was 4 point font 4 point font and the terms of the release were in smaller font); the release was outlined in a box; the heading was all caps, in bold type and read **"RELEASE AND WAIVER OF LIABILITY AND INDEMNITY AGREEMENT"**; and above the signature line appeared the caption in all caps, bold-faced centered and underlined type the following statement **"I UNDERSTAND MOTORCYCLE RACING IS DANGEROUS. YES, I HAVE READ THIS RELEASE."** The court did not accept the argument that the release was conspicuous because of its small contrasting type. "Where a party is not able to know what the contract terms are because they are unreadable, as a matter of law the exculpatory clause will not be enforced."

See Greer and Collier, *The Conspicuousness Requirement: Litigating and Drafting Contractual Indemnity Provisions in Texas After Dresser Industries, Inc. v. Page Petroleum, Inc.*, 35 SO. TEX. L. REV. 243 (1994) for an analysis of whether the Texas UCC might allow such provisions to be enforced, even if not "conspicuous," due to custom and trade practice prevailing in the industry in which the provision is used. *Also see* the Greer and Collier Article at page 257 for an interesting analysis of whether the Texas UCC quoted above is misquoted by placing the printed heading in "ALL CAPITALS" as opposed to "Initial Capitals." *See generally,* Baker, *Special Project: Article Two Warranties in Commercial Transactions*, 64 CORNELL L. REV. 30, 182-87 (1978); and Kistler, Note, *U.C.C. Article Two Warranty Disclaimers and the "Conspicuousness" Requirement of Section 2-316,* 43 MERCER L. REV. 943, 946-55 (1992). It is argued in White, *Winding Your Way Through the Texas Oilfield Anti-Indemnity Statute, the Fair Notice Requirements and Other Indemnity Related Issues*, 37 S. TEX. L. REV. 161, 174-75 (1996) that the Texas Supreme Court by noting "**actual** notice or knowledge" as an exception to the "fair notice requirements", which include not only the conspicuousness requirement but also the express negligence doctrine, **may** in the future hold that an Indemnifying Person is charged with **constructive** knowledge that the scope of an indemnity covers the Indemnified Person's negligence, even though the indemnity contained in the contract does not expressly state that it includes the Indemnified Person's negligence. White comments:

> It is interesting to note, however, that immediately after stating that actual knowledge overrides the question of conspicuousness, the *Cate* court then discussed, by way of example, provisions of the Texas Uniform Commercial Code that allow a party to disclaim implied warranties orally or by ways other than by a conspicuous written disclaimer, such as through 18a course of dealing, course of performance, or usage of trade. [Citing *Cate*, 790 S.W.2d at 562.]. These three instances, however, are really examples of when it is reasonable to impute constructive knowledge on a party.... If the Texas Supreme Court were to apply this same analysis with regard to the exception to the "fair notice" requirements, then **usage of trade** would certainly be the most interesting of the examples cited. Usage of trade may allow an indemnitee to prove "actual notice or knowledge" of the indemnitor with regard to an indemnity provision that did not otherwise comply with the express negligence doctrine and/or the conspicuousness requirement. This would not be accomplished by proving what the indemnitor subjectively knew of the content and the meaning of the indemnity agreement, but, instead, by looking to the general industry practices and determining what the indemnitor should have known. Of course, the "fair notice" requirements, themselves, are constructive notice requirements - if the requirements are complied with, then the court will essentially determine that the party against whom the provisions are being applied should have seen and understood such provisions, regardless of what the party actually saw or understood. *White*, at 175.

Recently, the Supreme Court has indicated that it might look to other factors to excuse a drafter's failure to make such a provision "conspicuous". The Supreme Court in *Green International, Inc. v. Solis*, 951 S.W.2d 384 (Tex. 1997) in holding that the fair notice requirements in *Dresser* did not apply to "no-damages-for-delay" provisions in construction contracts noted that the public policy behind the fair notice requirement of "conspicuousness" was not as strong in a case where the parties were experienced contractors familiar with the industry custom of allocating risk for delays. The court stated

> Furthermore, the concerns underlying the *Dresser* [853 S.W.2d 505 (Tex. 1993)-see discussion of releases at **Art. IV Exculpation and Limitation of Liability Provisions and Releases**] opinion are not present in this case. In *Dresser,* this Court was concerned with the injustice arising when a contracting party buries a provision substantially releasing itself from its own negligence in a way that is inconspicuous and does not provide fair notice to the other party. In the present case, there is no such injustice. Instead, both Green and Solis were experienced contractors familiar with the industry custom of allocating risk for delays.

The court did not state whether the parties actually knew of the presence of the provision in the contracts.

The "no-damages-for-delay" type of clause, according to the Court, does not involve the extraordinary shifting of risks of the type described in *Dresser.* It is not an indemnity because it doesn't shift the risk for third party claims. It is not a release because it doesn't extinguish a claim or cause of action. It is merely a shift in the economic consequences of a delay.

However, actual notice of the indemnity and risk allocation provisions cannot create a risk shifting provision where none exists and does not make enforceable an indemnity provision that does not meet the express negligence test in the first place. *DDD*

Energy, Inc. v. Veritas DGC Land, Inc., 60 S.W.3d 880 (Tex.App.-Houston [14th Dist.]2001, *no writ*).

Drafting: The following factors have been listed by the above cited cases as supporting a finding that the provision is not conspicuous: the provision is hidden on the reverse side of the contract; the face of the contract includes multiple paragraphs of hundreds of words in regular size type, without color or other distinguishing characteristics; incorporating numerous paragraphs on the reverse side of the contract, the reverse side of the contract includes multiple paragraphs of hundreds of words, all in regular size or reduced type, without color or other distinguishing characteristics, and contains the indemnity provision; the indemnity provision is in a paragraph with a heading not indicating the nature of the provision as an indemnity; the indemnity provision is not separated from the surrounding unrelated provisions.

Section 1.201(10) of the Texas UCC lists the following as being available to make a provision conspicuous: bold-face type, increased-size type, capital letters, and different colored type. Other statutes use the following to make an item conspicuous: underlining--§ 35.53(b) *Notice of Law; Dispute Resolution Forum Applicable to Contract* TEX. BUS & COMM. CODE (Vernon Supp. Pamphlet 2002) authorizing **CAPITALIZATION or underlining** as a method to make a choice of non-Texas law provision conspicuous; putting a box around the provision--Federal Truth-in-Lending Act, *also see Singleton v. LaCoure,* 712 S.W.2d 757, 758-59 (Tex. App.--Houston [14th Dist.] 1986, *writ ref'd n.r.e.*); *Architectural Aluminum Corp. v. Macarr, Inc.* 333 N.Y.S.2d 818, 823 (N.Y. County Sup. Ct. 1972).

Greer and Collier recommend against the use of *italics* as the sole means of making an indemnity look conspicuous. *See* Greer and Collier, *The Conspicuousness Requirement: Litigating and Drafting Contractual Indemnity Provisions in Texas After Dresser Industries, Inc. v. Page Petroleum, Inc.*, 35 SO. TEX. L. REV. 243, 265-67 (1994) citing *Office Supply Co. v. Basic/Four Corp.,* 538 F. Supp. 776, 783-84 (E.D. Wis. 1982); *De Lamar Motor Co. v. White,* 460 S.W.2d 802, 804 (Ark. 1970) and J. White & R. Summers, UNIFORM COMMERCIAL CODE, PRACTITIONER'S EDITION 574, 575 (3d ed. 1988).

How "conspicuous" is conspicuous? For example, in an Oregon case involving a UCC disclaimer, the disclaimer was on both the front and back of the agreement. On the front it was captioned "Warranty Disclaimer" in "bold 8 point blue type" with its text in contrasting 7 point type which differed from the "fine print" (6 point type) in the agreement--but not by much. Did that suffice? It did not. The court found the front of the agreement a "hodgepodge" of various print sizes and other attention--getting devices including "bold type, capital letters, red type and reverse lettering" such that the disclaimer language could not be said to be conspicuous, at least not in this general stew. What was clear from the front was that the back of the agreement was to be read. It provided "READ BOTH SIDES BEFORE SIGNING." The disclaimer was repeated on the back side. The court found it failed to be conspicuous. The language on the rear was all in "the same, faint type, with identical headings." *Anderson v. Ashland Rental, Inc.,* 858 P.2d 470 (Or. App. 1993); 24 UCC Rep.2d 34 (1993); *also see Laudisio v. Amoco Oil Co.,* 437 N.Y.S.2d 502, 505-06 (N.Y. Sup. Ct. 1981).

Greer and Collier make the following 11 drafting suggestions:

1. Make the indemnity provision look noticeable.

2. Avoid using italics, lighter-colored type, same-typed print or smaller print.

3. Emphasize the entire paragraph--not just portions.

4. Do not overuse conspicuousness techniques.

5. Avoid putting indemnities on the backs of contracts.

6. Make indemnities more conspicuous by placement at the beginning or end of the contract.

7. Do not use misleading headings.

8. Use headings.

9. Do not surround indemnities with unrelated terms.

10. The less formal the contract, the greater the need for conspicuousness.

11. Initial the indemnity paragraphs.

d. Actual Notice. The conspicuousness requirement is not applicable when the Indemnified Person establishes that the Indemnifying Person possesses actual notice or knowledge of the indemnity agreement. *Dresser Industries, Inc. v. Page Petroleum, Inc.,* 853 S.W.2d 505, 508 (Tex. 1993), *citing generally Cate v. Dover Corp.,* 790 S.W.2d 550, 561 (Tex. 1990). *See McGehee v. Certainteed Corp.,* 101 F.3d 1078 (5th Cir. (Tex.) 1996) remanding case for trial on actual knowledge of inclusion of an inconspicuous indemnity; *Coastal Transport Co. v. Crown Central Petroleum Corp.*, 20 S.W.3d 119 (Tex.App.-Houston [14th Dist.] 2000, *no writ*)-admission that signing party read the agreement sufficient to establish actual notice; *Goodyear Tire & Rubber Co. v. Jefferson Constr. Co.,* 565 S.W.2d 916, 919 (Tex. 1978), *overruled on other grounds by Dresser Indus., Inc.*, 853 S.W.2d at 509; *Douglas Cablevision v. SWEPCO*, 992 S.W. 2d 503 (Tex.App.-Texarkana 1999, *no writ*).

2. Consideration. For example, it has been held that an agreement to forbear filing a cross action against the Indemnifying Person in consideration of the Indemnifying Person's promise to hold the indemnified

person harmless and protect the indemnified person against judgment is adequate consideration to support an indemnity contract. *Russell v. Lemons*, 205 S.W.2d 629 (Tex. Civ. App.--Amarillo 1947, *writ ref'd n.r.e.*).

3. Promise. It is not necessary that the words "indemnify" or "indemnity" be used or even that the promise be in writing. 14 TEX. JUR. 3d *Contribution and Indemnification* § 14 Form (1997); 26 TEX. JUR. 2d *Statute of Frauds* § 29.

4. Statutory Limits on Indemnity. A contract of indemnity is not against public policy even if the Indemnified Person is indemnified against its own negligence, except if there is a specific statute declaring such a contract is void.

a. Architects and Engineers. Contractual indemnity for malpractice by architects and engineers is void. Only insurance companies may indemnify architects and engineers for malpractice pursuant to professional liability policies. TEX. CIV. PRAC. & REM. CODE ANN. §§ 130.001-.005 (Vernon Supp. 2003). This statute does not prevent a negligent contractor from indemnifying a non-negligent architect. *Foster, Henry, Henry, & Thorpe, Inc. v. J. T. Const. Co., Inc.*, 808 S.W.2d 139 (Tex. App.--El Paso 1991, *writ denied*). This Section was amended effective September 1, 2001, to also provide that:

> A covenant or promise in, in connection with, or collateral to a construction contract other than a contract for a single family or multifamily residence is void and unenforceable if the covenant or promise provides for a registered architect or licensed engineer whose engineering or architectural design services are the subject of the construction contract to indemnify or hold harmless an owner or owner's agent or employee from liability for damage that is caused by or results from the negligence of an owner or an owner's agent or employee.

b. DTPA. Indemnity rights are not prohibited by the Texas Deceptive Trade Practices Act. TEX. BUS. & COMM. CODE ANN. § 17.555 (Vernon 1987) provides "[a] person against whom an action has been brought" under the DTPA can assert all contribution or indemnity rights available under statutory or common law. *Also see Plas-Tex, Inc. v. U.S. Steel Corp.*, 772 S.W.2d 442 (Tex. 1989); *Aviation Office of America, Inc. v. Alexander & Alexander of Texas, Inc.*, 751 S.W.2d 179, 180 (Tex. 1988) (*per curiam*).

c. Oil and Gas Service Contracts. Indemnity contracts in oil and gas service contracts are void as against public policy unless certain statutory requirements are met. TEX. CIV. PRAC. & REM. CODE ANN. §§ 127.001-.007 (Vernon 1997). This statute is known as the Texas Oilfield Anti-Indemnity Statute; this statute, formerly TEX. REV. CIV. STAT. ANN. Art. 2212b, was originally enacted in 1973, and amended in 1979. Article 2212b was recodified as Chapter 127 of the Civil Practice and Remedies Code in 1985, and amended again in 1989. *See* White, *Winding Your Way Through the Texas Oilfield Anti-Indemnity Statute, the Fair Notice Requirements and Other Indemnity Related Issues*, 37 S. TEX. L. REV. 161 (1996); Powell, *Indemnity and Insurance Provisions in Oil and Gas Agreements,* Advanced Oil, Gas and Mineral Course (State Bar of Texas 1996); Tade, *Indemnification - Who Wins, Who Loses Under Texas, Louisiana and Maritime Law*, 20TH ANNUAL OIL, GAS & MINERAL LAW INSTITUTE 12-21 (UNIV. TEX. 1994); Tade, *Texas Anti-Indemnity Law Update*, 53 TEX. B.J. 107 (1990). *Also see Transworld Drilling Co. v. Levingston Shipbuilding*, 693 S.W.2d 19, 23 (Tex. App.--Beaumont 1985, *no writ*) for a review of the types of contracts governed by this statute. The Texas Oilfield Anti-Indemnity Statute provides that an agreement pertaining to an oil and gas well is void if it purports to indemnify a party from loss or liability for damage arising out of its own negligence.

Prior to the enactment of Article 2212b in 1973, many oil companies and oil well operators had imposed "hold harmless" agreements on oil well drilling and service contractors to indemnify the oil companies and operators for losses caused by the negligence of the drilling contractor, and often for the negligence of the oil company, operator and third parties as well. Many believed that such agreements placed an undue financial burden on what were perceived to be small contractors with less bargaining power than the oil companies and operators with whom they were negotiating contracts. *See* HOUSE INTERIM STUDY COMMITTEE ON HOLD HARMLESS AGREEMENTS, REPORT, 63rd Leg., at 3-8 (1973). The legislature enacted the Oilfield Anti-Indemnity Statute in 1973 to cure this perceived inequity by prohibiting agreements pertaining to oil and gas wells that indemnify a party for its own negligence.

(1) Void Agreements. Section 127.003 TEX. CIV. PRAC. & REM. CODE ANN. (Vernon 1997) provides

> (a) Except as otherwise provided by this chapter, a covenant, promise, agreement, or understanding contained in, collateral to, or affecting an agreement pertaining to a **well for oil, gas, or water or to a mine for a mineral** is void if it purports to indemnify a person against loss or liability for damage that:
>
> (1) is caused by or results from the sole or concurrent negligence of the indemnitee, his agent or employee, or an individual contractor directly responsible to the indemnitee; and
>
> (2) arises from:
>
> (A) personal injury or death;
> (B) property damage; or
> (C) any other loss, damage, or expenses that arises from personal injury, death, or property injury.

(2) Excluded Activities.

(a) Joint Operating Agreements. Following the ruling in *Haring v. Bay Rock Corp.*, 773 S.W.2d 676 (Tex. App.--San Antonio 1989, *no writ*), oil operators were successful in having joint operating agreements excluded from the Oilfield Anti- Indemnity Statute and in creating a legislative exception to the court-created express negligence test.

Section 127.002(c) adopted in 1991 (Vernon 1997) provides:

> (c) The legislature finds that joint operating agreement provisions for the sharing of costs or losses arising from joint activities, including costs or losses attributable to the negligent acts or omissions of any party conducting the joint activity:
>
> > (1) are commonly understood, accepted, and desired by the parties to joint operating agreements;
> >
> > (2) encourage mineral development;
> >
> > (3) are not against the public policy of this state; and
> >
> > (4) are enforceable unless those costs or losses are expressly excluded by written agreement.

Prior to the adoption of this amendment, great concern was expressed among oil operators that the standard provisions exculpating and indemnifying the operator by the non-operators, contained in the model form joint operating agreement published by the American Association of Petroleum Landmen ("*A.A.P.L.*"), would fail the express negligence test. The A.A.P.L. form provides that the operator, in its capacity as operator, is to have no liability to the other parties for losses or liabilities, unless such losses or liabilities result from the gross negligence or willful misconduct of the operator. The A.A.P.L. model form provides that costs attributable to the negligence of the operator are to be borne and paid by each party according to its interest. Even though the A.A.P.L. form was revised in 1989, these provisions dealing with release and indemnification of the operator were not revised to bring the form into compliance with the Texas express negligence rule. A. Derman, *The New and Improved 1989 Joint Operating Agreement: A Working Manual,* NATURAL RESOURCES, ENERGY AND ENVIRONMENTAL LAW SECTION, MONOGRAPH SERIES No. 15. A.A.P.L. Form 610-1989 Model Form Operating Agreement; A.A.P.L. Form 610-1982 Model Form Operating Agreement; A.A.P.L. Form 610-1977 Model Form Operating Agreement; and A.A.P.L. Form 610-1956 Model Form Operating Agreement. Darden, *In Support of the Operator Liability Provision of the AAPL Model Form Joint Operating Agreement: A Pre-Emptive Strike Against Possible Claims Made Under Page Petroleum, Inc. v. Dresser Industries, Inc.,* 18 TEX. ST. B. SEC. REP. OIL GAS & MIN. L. 20 (1994). However, there still may exist an issue as to whether these exculpatory and indemnity provisions of the Joint Operating Agreement must still meet the fair notice requirements, and if they do not, then whether they are enforceable. White, *Winding Your Way Through the Texas Oilfield Anti-Indemnity Statute, the Fair Notice Requirements and Other Indemnity Related Issues*, 37 S. TEX. L. REV. 161, 176-77 (1996).

(b) Gas Pipelines. "Well or mine service" is defined in § 127.001(4) (Vernon 1997). Gas pipelines and "fixed associated facilities" are expressly excluded from the prohibitions of the statute by being excluded from the definition of "well or mine service." Section 127.001(4)(B).

(3) Permitted Indemnity: "Indemnity Supported by Insurance". Section 127.005 TEX. CIV. PRAC. & REM. CODE ANN. (Vernon Supp. 2002) permits specified forms of indemnity if supported by specifically permitted levels of insurance. Section 127.005 as amended in 1995 provides

> (a) This Chapter does not apply to an agreement that provides for indemnity if the parties agree in writing that the indemnity obligation will be supported by liability insurance coverage to be furnished by the indemnitor subject to the limitations specified in Subsection (b) or (c).
>
> (b) With respect to a *mutual indemnity obligation* (defined below), the indemnity obligation is limited to the extent of the coverage and dollar limits of insurance or qualified self-insurance each party as indemnitor has agreed to obtain for the benefit as to the other party as indemnitee.
>
> (c) With respect to a *unilateral indemnity obligation* (defined below), the amount of insurance required may not exceed $500,000.

Section 127.001 (Vernon 1997) contains the following definitions of "mutual indemnity obligation" and "unilateral indemnity obligation":

> (3) "Mutual indemnity obligation" means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which the parties agree to indemnify each other and each other's contractors and their employees against loss, liability, or damages arising in connection with bodily injury, death, and damage to property of the respective employees, contractors or their employees, and invitees of each party arising out of or resulting from the performance of the agreement.
> ...
> (6) "Unilateral indemnity obligation" means an indemnity obligation in an agreement pertaining to a well for oil, gas, or water or to a mine for a mineral in which one of the parties as indemnitor agrees to indemnify the other party as indemnitee with respect to claims for personal injury or death to the indemnitor's employees or agents or to the employees or agents of the indemnitor's contractors but in which the indemnitee does not make a reciprocal indemnity to the indemnitor.

The Fifth Circuit in *Campbell v. Sonat Offshore Drilling, Inc.,* 979 F.2d 1115 (5th Cir. 1992) held that under the Texas Oilfield Anti-Indemnity Act, an indemnitee may collect indemnity up to the amount of insurance *actually obtained* by the indemnitor (in this case the indemnitor had $10,000,000 insurance coverage even though the Texas Oilfield Anti-Indemnity Act prohibited *requiring* the indemnitor to carry in excess of $300,000 in insurance). In this case, Union Texas Petroleum Corporation ("*UTP*") hired a drilling vessel from Sonat Offshore Drilling ("*Sonat*") to drill a well on the outer continental shelf off the coast of Louisiana. UTP also entered into an

agreement with Frank's Casing Crew and Rental Tools, Inc. ("*Frank's*") to perform casing and other services on board the drilling vessel. Campbell, an employee of Frank's, was injured while transferring to Sonat's drilling vessel from a supply boat hired by UTP. After Campbell sued UTP and Sonat, UTP filed a third-party complaint against Frank's and Frank's insurers seeking indemnity pursuant to the indemnity provision contained in the purchase order between UTP and Frank's.

The "indemnity supported by insurance" exception to the prohibition against indemnities does not apply to agreements with respect to the purchase, gathering, storage, or transportation of oil, gas, brine water, fresh water, produced water, petroleum products, or other liquid commodities. In other words, no indemnity against one's own negligence is allowed in these instances. Section 127.005(a) (Vernon Supp. 2002).

Only Texas, Louisiana, New Mexico and Wyoming have anti- indemnity statutes directed particularly at oil and gas operations. *See generally* Battiato & Gilbertson, *The Changing Insurance Market-- Who Will Bear the Risks?*, 32 ROCKY MTN. MIN.L. INST. § 17.04 at 17- 16 (1986); Owen L. Anderson, *The Anatomy of an Oil and Gas Drilling Contract*, 25 TULS. L.J. 359, 421-31 (1990).

E. Rules of Construction.

1. General Rules.

a. Intent. A contract of indemnity is read, as any other contract, to ascertain the intent of the parties. *Ohio Oil Co. v. Smith*, 365 S.W.2d 621, 627 (Tex. 1963); *Spence & Howe Const. Co. v. Gulf Oil Corp.*, 365 S.W.2d 631, 637 (Tex. 1963); *Mitchell's, Inc. v. Friedman*, 303 S.W.2d 775, 777-78 (Tex. 1957); and *Sun Oil Co. v. Renshaw Well Service, Inc.*, 571 S.W.2d 64, 68 (Tex. Civ. App.--Tyler 1978, *writ ref'd n.r.e.*).

b. *Strictissimi Juris*. Once the intent of the parties is ascertained, the doctrine of *strictissimi juris* is applied to prevent the Indemnifying Persons's liability from being extended beyond the terms of the agreement. *Liberty Steel Co. v. Guardian Title Co. of Houston, Inc.*, 713 S.W.2d 358, 360 (Tex. App.--Dallas 1986, *no writ*).

2. Elements of an Indemnity. An indemnity is comprised of the following components: (a) the "indemnitors" (the "***Indemnifying Person***"), (b) the "indemnitees" (the "***Indemnified Persons***"), (c) the indemnified events, acts or omissions (the "***Indemnified Matters***"), (a) the indemnified liabilities (the "***Indemnified Liabilities***"), and (b) any excluded matters or excluded liabilities (the "***Excluded Matters***").

a. Indemnifying Persons. In *Jones v. San Angelo Nat. Bank*, 518 S.W.2d 622 (Tex. Civ. App.--Beaumont 1974, *writ ref'd n.r.e.*) the court found that a corporation was not an Indemnifying Person and refused to require the corporation to make contribution to a shareholder for one-half the amount paid by such shareholder to the other shareholder in connection with the paying shareholder's satisfaction of a debt of the corporation pursuant to a corporate dissolution agreement.

(1) Multiple Indemnifying Persons: Rights of Contribution. When two persons separately indemnify a third party, then as between themselves, each is liable for only half. *Hobbs v. Teledyne Movible Offshore, Inc.,* 632 F.2d 1238, 1241 (5th Cir. Unit A 1980)--applying Louisiana law.

(2) Indemnifying an Indemnifying Person: No Right of Contribution. The court in *Campbell v. Sonat Offshore Drilling, Inc.*, 27 F.3d 185 (5th Cir. 1994) rejected the argument of Frank's Casing Crews and Rental Tools that it could obtain contribution from Union Texas Petroleum in a case where both Frank's and Union had indemnity agreements naming a liable third party (Sonat Offshore Drilling) as an Indemnified Person. In an earlier case, *Campbell v. Sonat Offshore Drilling, Inc.*, 979 F.2d 1115 (5th Cir. 1992) ("*Campbell I*") the court found that Frank was obligated to indemnify Sonat Offshore Drilling for an injury sustained by Frank's employee (Campbell). *See* discussion of *Campbell I* on page 43 hereof. In this second case ("*Campbell II*") Frank was attempting to share its liability with Union Texas Petroleum since both Frank and Union Texas Petroleum had indemnified Sonat for injuries to Frank's employees.

The court in *Campbell II* found, however, that Frank's indemnity, which was contained in its contract with Union Texas Petroleum, expressly provided that Frank indemnified *both* Sonat and Union Texas Petroleum for injuries to Frank's employee. Union Texas Petroleum did not have to make contribution despite its separate indemnity undertaking in the contract between Union Texas Petroleum and Sonat.

These cases involved injuries sustained by Campbell, an employee of Frank's Casing Crews and Rental Tools, who was injured while transferring onto the jack-up drilling vessel owned by Sonat Offshore Drilling. Union Texas Petroleum had chartered Sonat's vessel and had agreed to indemnify Sonat for such injuries (the UTP/Sonat Contract). Frank's had agreed to indemnify Union Texas Petroleum and Sonat against liability for injuries to Frank's employees in its contract with UTP (the UTP/Frank's Contract).

Also see Foreman v. Exxon Corp., 770 F.2d 490, 498 n.13 (5th Cir. 1985) and *Corbitt v. Diamond M. Drilling Co.,* 654 F.2d 329 (5th Cir. Unit A 1981).

b. Indemnified Persons.

(1) Direct Beneficiaries.

(a) Primary Indemnified Party. Indemnification clauses typically name a primary party and secondary persons as being Indemnified Persons. For example, an owner may be named as the primary Indemnified Person in a construction contract requiring the contractor to indemnify the owner for liabilities arising out of the contractor's construction activities.

(b) Secondary Indemnified Persons. In addition to naming the owner as the primary Indemnified Person, the owner may also

require that the scope of the indemnity also include liabilities of other persons by listing them as "additional" Indemnified Persons.

Provision:

> "Indemnified Persons" shall include (a) the Owner, the Owner's partners, affiliated companies of Owner or of any partner of Owner, (b) Owner's construction lender, (c) the Architect, and (d) as to each of the persons listed in (a)-(c) the following persons: each of such person's respective partners, partners of their partners, and any successors, assigns, heirs, personal representatives, devisees, agents, stockholders, officers, directors, employees, and affiliates of any of the persons listed in this clause (d).

Other examples of contractual enlargements of direct beneficiaries of an indemnity are "additional named insured" endorsements to liability policies and "dual obligee riders" on performance bonds.

The importance of specifically designating in the indemnity clause all of the persons intended to be Indemnified Persons is emphasized by *Melvin Green, Inc. v. Questor Drilling Corp.*, 946 S.W.2d 907 (Tex.App.--Amarillo 1997, *no writ*) where the court found that a **consultant** was not an Indemnified Person within the listing of indemnity clause covering the "Operator, its officers, directors, employees and joint owners". Other provisions of the IADC Drilling Bid Proposal and Daywork Drilling Contract specifically listed "consultants". For example, the provision defining "daywork" stated that "For purposes hereof the term 'daywork' means .... under the direction, supervision and control of Operator (which term is deemed to include an employee, agent, consultant or subcontractor engaged by Operator to direct drilling operations)."

An example where an Indemnified Person was not fully protected is the case of *Amerada Hess Corp. v. Wood Group Production Technology*, 30 S.W.3d 5 (Tex.App. [14th Dist.] 2000, *writ denied*). In *Hess* the court found that a portion of the attorney's fees Hess incurred in defending a suit brought by an injured employee of the Wood Group was not covered by the Wood Group's indemnity. Hess sought and obtained reimbursement from the Wood Group for the $200,000 it had paid to settle the claim, but was denied the right to recover 100% of the $141,743.75 in attorney's fees it incurred in defending the claim. The trial court's finding that the $200,000 settlement of the claim was reasonable was upheld by the court of appeals despite the fact that another defendant (Graham) was released in the settlement agreement. The court found that the settlement amount was reasonable as to the potential liability of Hess alone. However, Hess in defending the claim, also was defending a claim against Graham for Graham's negligence. Hess had agreed to indemnify Graham. The Wood Group had indemnified Hess. The trial court held that the Wood Group indemnity did not include Hess' contractual obligation to indemnify Graham; and thus did not include the portion of Hess' fees incurred in defending Graham.

(2) Third Party and Incidental Beneficiaries.

(a) Bonds. Indemnity bonds usually are construed as contracts of indemnity not creating third party beneficiary rights to sue on bond protecting indemnitee of bond. *Fidelity & Deposit Co. of Maryland v. Reed*, 108 S.W.2d 939 (Tex. Civ. App.--San Antonio 1937, *no writ*); 10 TEX. JUR. 3d, *Bonds and Undertakings* (1980).

(b) Creditors. It has been held that creditors of the seller of a business are not third party beneficiaries of an "all bills paid" indemnity contained in a contract for the sale of a business so as to revive a claim otherwise barred by the statute of limitations. *House of Falcon, Inc. v. Gonzalez*, 583 S.W.2d 902 (Tex. Civ. App.--Corpus Christi 1979, *no writ*). A creditor of an Indemnified Person has been held to be merely an incidental beneficiary of an indemnity agreement and does not have the right to bring suit directly against the Indemnifying Person. *Hurley v. Lano International, Inc.*, 569 S.W.2d 602 (Tex. Civ. App.--Texarkana 1978, *writ ref'd n.r.e.*).

c. Indemnified Matters. The matters covered by the indemnity can included events, acts, and omissions of the Indemnified Persons and/or the Indemnifying Persons.

(1) Strict Construction Limiting Scope of Indemnified Matters. After the court has determined that an indemnity is intended, the doctrine of *strictissimi juris* or strict construction is used to prevent liability under the indemnity contract from being extended beyond the terms of the contract. Courts have stated that the Indemnifying Person is entitled to have the indemnity contract strictly construed in the Indemnifying Person's favor. *Smith v. Scott*, 261 S.W. 1089 (Tex. Civ. App.– Amarillo 1924, *no writ*); *Ohio Oil Co. v. Smith*, 365 S.W.2d 621 (Tex. 1963); and other cases discussed below. Courts examine the "event" to determine whether it is within the scope of Indemnified Matters.

The San Antonio court of appeals has held that an indemnity for one's own negligence also includes all shades and degrees of negligence, including one's own gross negligence. *Webb v. Lawson-Avila Const., Inc.,* 911 S.W.2d 457 (Tex. App.–San Antonio 1995, *writ dism'd by agreement*). *See discussion below* at **Article IIE2c(4)-Contractual Indemnity - Rules of Construction - Elements of Indemnity - Indemnified Matters - Contractual Exceptions** reviewing contractual exceptions for negligence as including an exception for one's own gross negligence.

(2) Conflicting Terms: Express Duty and Indemnity. Many times a contract containing an indemnity provision will also contain a duty provision or other covenant which conflicts with the indemnity provision. In such cases, the indemnity is strictly construed and effect is first given to the conflicting provision.

In *Eastman Kodak Co. v. Exxon Corp.*, 603 S.W.2d 208 (Tex. 1980), the supreme court found that there were conflicting provisions in the contract containing an indemnification provision. Damages resulted from

an explosion of a pipe line that transported propane to Kodak's facility. The contract contained both a provision requiring the Indemnifying Person to hold the oil company harmless from the oil company's own negligence, and a provision which placed responsibility for pipe line breakages on the oil company. The court was applying the "clear and unequivocal" test.

(3) Liabilities "Arising Out Of."

Indemnity provisions seek to tie the indemnified liability in some fashion to relationship between the Indemnified Person and the Indemnifying Person. The most common means of connection is to state that the liabilities indemnified "**arise out of**" some aspect of the relationship, such as indemnifying an owner, as the Indemnified Party, for bodily injuries or deaths "**arising out of the Work**" of a contractor.

Queries: Does the Indemnified Matter (liability) have to be "**proximately caused**" by the acts or omissions (negligence) of the Indemnifying Person? ...at least "**in part**" by the acts or omissions (negligence) of the Indemnifying Person?

The elements of a negligence cause of action are a duty, a breach of that duty, and damages proximately caused by the breach of duty. *Doe v. Boys Clubs of Greater Dallas, Inc.*, 907 S.W.2d 472, 477 (Tex. 1995). The components of proximate cause are "cause-in-fact" and "foreseeability." The test for cause-in-fact is whether the negligent act or omission was a substantial factor in bringing about injury, without which the harm would not have occurred. "Foreseeability" requires that a person of ordinary intelligence should have anticipated the danger created by a negligent act or omission. It asks whether the injury might reasonably have been contemplated as a result of the defendant's conduct.

The court in *Sieber & Callicutt, Inc. v. La Gloria*, 66 S.W.3d. 340 (Tex.App.-Tyler 2001, *no writ*) found, in a case where the negligence of the Indemnified Party (La Gloria) and the negligence of the Indemnifying Party (Sieber & Callicutt) was determined to be equal, that the negligence of the Indemnifying Party was a "**substantial factor**" and "**a proximate cause**" of the liability although not the only factor in causing the Indemnified Matter (liability to the estate of a deceased employee of the Indemnified Party, La Gloria). La Gloria settled the wrongful death action and sued Sieber & Callicutt on Sieber & Callicutt's indemnity in its maintenance contract with La Gloria. The trial court found that there was a reasonable risk that La Gloria would have been found grossly negligent (the manway cover was in extreme disrepair), Sieber & Callicutt also was negligent (by running a hot water line into the tank and not advising La Gloria), and La Gloria and Sieber were equally negligent. The Indemnifying Party (Sieber & Callicutt) urged the court to find that the "**arising in any manner**" language in the indemnity did not "provide a lower causal connection than proximate cause" and thus it should not be required to indemnify La Gloria, even for Sieber's proportion of causation. The court rejected Sieber's argument noting that the trial court found that Sieber was negligent and that a component of negligence is proximate cause. Since the indemnity provision expressly provided for Sieber to indemnify La Gloria for Sieber's proportionate share of liability, Sieber was liable to La Gloria for one-half of the settlement.

Provision:

> Contractor (Sieber & Calicutt) agrees to hold harmless and unconditionally indemnify La Gloria, its directors, officers, agents, representatives and employees against and for all liability, costs and expenses, claims and damages which La Gloria at any time suffer or sustain or become liable for by reason of any accidents, damages or injuries either to the persons or property or both, of Contractor, its subcontractors and suppliers, or to the persons or property of La Gloria, its subcontractors and suppliers, **arising in any manner** from the Work performed hereunder, including but not limited to any negligent act or omission of La Gloria, its directors, officers, agents, representatives or employees, provided however, that if the negligence of La Gloria shall be found to be greater than or equal to the comparative negligence of the Contractor, then the Contractor shall only be liable to La Gloria to the extent of the Contractor's own negligence.

The phrase "**arising out of**" has been the subject of recent cases. In *General Agents v. Arredondo*, 52 S.W.3d 762 (Tex.App.-San Antonio [4th Dist.] 2001, *no writ*) the court broadly construed the exclusion for "injuries **arising out of** a contractor's and subcontractor's operations" contained in a contractor's commercial general liability policy as not being limited to injuries caused by an act of the contractor or subcontractor. The court found that "all that is required is a "**causal connection**". The court cited the following authorities for this conclusion:

> *Cf. Mid-Century Ins. Co. v. Lindsey*, 997 S.W.2d 153, 156-57 (Tex. 1999)("For liability to 'arise out of' in the context of an 'additional insured' endorsement does not require that named insured's act caused accident.") Indeed, in more recent cases, the Fifth Circuit has recognized that the phrase "arising out of" is "understood to mean '**originating from,**' '**having its origin in,**' '**growing out of,**' or '**flowing from**.'" *American States Ins. Co. v. Bailey,* 133 F.3d 363, 370 (5th Cir. 1998)(quoting *Red Ball Motor Freight, Inc. v. Employers Mut. Liab. Ins. Co.*, 189 F.2d 374, 378 (5th Cir. 1951)). Thus, a "claim need only bear an '**incidental relationship**' to the excluded injury for the policy's exclusion to apply." *Bailey*, 13 F.3d at 370 (quoting *Continental Cas. Co. v. Richmond*, 763 F.2d 1076, 1080-81 (9th Cir. 1985)."

The concept of liability being a covered liability as one "**arising out of**" the "***work***" or *"**operations**"* is an issue that has been litigated in the context of coverage of an additional insured's negligence under an additional insured endorsement. *See* the discussion of **IIIB Coordination with Insurance Coverage-Additional Insured Status** for cases addressing the issue of whether an additional insured endorsement on a liability policy covers an additional insured's negligence as one "**arising out of the operations**" of the named insured.

(4) Injuries.

(a) "Injuries". The failure of the indemnity provision to specifically cover "personal injuries" was held to be fatal, even though the indemnity provision otherwise would meet the express negligence test, in *Ard v. Gemini Exploration Co.*, 894 S.W.2d 11 (Tex. Civ. App.-- Houston [14th Dist.] 1994, *writ denied*).

(b) Injuries To Indemnifying Person. An indemnity provision whereby a contractor indemnified a railroad against liability for injuries to the contractor's agents and employees, but did not mention injuries to the contractor, did not indemnify against injuries to the contractor. The Indemnified Matters did not include injuries to the Indemnifying Person, the contractor. *International G.N.R. Co. v. Lucas*, 70 S.W.2d 226 (Tex. Civ. App.--Texarkana 1934), *rev'd on other grounds* 99 S.W.2d 297 (Tex. Comm. 1936), *later app*, 123 S.W.2d 760 (Tex. Civ. App.-- Eastland 1938, *writ ref'd*), *cert. denied* 308 U.S. 573 (1939) *and aff'd in part and rev'd in part on other grounds* 100 S.W.2d 97 (Tex. Comm. 1937).

(c) Injuries To Employee of Indemnified Person. In one case, an indemnity provision in a lease whereby the lessee undertook to indemnify the lessor against liabilities arising out of injuries to "persons whomsoever" has been construed rather broadly by a court to include the employees of the lessor. *Gulf, C. & S. F. R. Co. v. McBride*, 309 S.W.2d 846, *rev'd on other grounds*, 322 S.W.2d 492 (Tex. 1958). *Also see Faulk Management Services v. Lufkin Industries, Inc.,* 905 S.W.2d 476 (Tex. App.-- Beaumont 1995, *writ denied*).

(d) Injuries To Employee of Indemnifying Person. The Texas Supreme Court in *Enserch Corp. v. Parker*, 794 S.W.2d 2, 7 (Tex. 1990) construed the following reference to "death to persons" to be specific enough to overcome the Workers' Compensation Bar in holding that an employer had contractually assumed liability to indemnify a third party (Enserch) for liabilities arising out of the concurrent negligence of the third party (the third party's negligent supervision of the employer's work):

Provision:

> (Christie) assumes entire responsibility and liability for any claim or actions based on or arising out of injuries, including death **to persons** ... incidental to the performance of this contract by (Christie)... . (Court's emphasis in bold.)

A full statement of the indemnity clause and a discussion of the court's finding that this clause met the express negligence test is found above in the discussion of the cases applying *Ethyl*.

The supreme court found that this language was sufficient to refer to employees of the Indemnifying Person (Christie) and therefore met the requirements of the Texas Workers' Compensation Act that permits "an express agreement in writing assuming liability" by an employer for injuries to its employees. The court cited with approval the court of appeals' decision in *Verson Allsteel Press Co. v. Carrier Corp.*, 718 S.W.2d 300 (Tex. App.--Tyler 1985, *writ ref'd n.r.e.*) which held the following similar language sufficient to overcome the Workers' Compensation Bar:

Provision:

> (Carrier) ... covenants to indemnify and hold harmless Verson ... from and against any and all loss, damage, expense, claims, suits or liability which Verson or any of its employees may sustain or incur ... for or by reason of any injury to or death of **any person or persons** or damage to any property, arising out of... any claimed inadequate or insufficient safeguards or safety devices. (*Enserch* court's emphasis.)

Id. at 301.

The supreme court in *Enserch* distinguished the following provision in *Port Royal Dev. v. Braselton Constr. Co.*, 716 S.W.2d 630, 632 (Tex. App.--Corpus Christi 1986, *writ ref'd n.r.e.*) on the grounds that the language expressly stated that the Indemnifying Person would not indemnify the Indemnified Person for the Indemnified Person's own negligence:

Provision: The subcontractor agreed to indemnify the contractor from liability

> for or on account of injury to or death of person or persons ... occurring by reason of or arising out of the act or (negligence) of **Subcontractor** ... **except the act or (negligence) of the Contractor** in connection with performance of this Contract. (Emphasis added by *Enserch* court.)

The Indemnified Matters did not include injuries to an employee of the Indemnifying Person due to the negligence of the Indemnified Person.

In *Fisher Constr. Co. v. Riggs*, 320 S.W.2d 200, 210 (Tex. Civ. App.--Houston 1959), *rev'd on other grounds*, 325 S.W.2d 126 (Tex. 1959), *and vacated on other grounds* 326 S.W.2d 915 (Tex. Civ. App.-- Houston 1959, *no writ*), the court of appeals found that a subcontractor was required to indemnify a contractor for contractor's negligent acts that injured the subcontractor's employees pursuant to indemnity which specifically included injuries to subcontractor's employees; the subcontractor's employees were considered to be "business invitees" in the portion of the construction site where injury occurred.

The Texarkana Court of Appeals in *Texas Utilities Electric Co. v. Babcock & Wilcox,* 893 S.W.2d 739 (Tex. App.--Texarkana 1995, *no writ*) found that the following indemnity provision did **not** cover injuries to an employee of Flour Daniel, a contractor employed by Texas Utilities, the Indemnified Person:

Provision:

> [Babcock & Wilcox agree to indemnify Texas Utilities for claims against Texas Utilities for damages arising from] personal injury or death or damage to property of Company's [Babcock's] agents, servants and employees, as well as the agents, servants, and employees of Company's [Babcock's] subcontractor, whether or not arising

from sole or concurrent negligence or fault of Purchaser [Texas Utilities].

(e) To Independent Contractor of Indemnifying Person. It has been held that an indemnity provision which clearly limited a contractor's obligation to indemnify the property owner for injuries sustained by the contractor's and its subcontractor's "*employees*" did **not** cover an injury sustained by a person while serving as an independent contractor, notwithstanding that the individual was hired, as well as paid, by the contractor. *Ideal Lease Service, Inc. v. Amoco Production Co.*, 662 S.W.2d 951 (Tex. 1983).

(5) Damages. In drafting the classes of liabilities covered by an indemnity care should be given to the scope of covered items. For example, are "**punitive damages**" of the Indemnified Person to be covered? Are the punitive damages of an employee or an agent covered, if the employer is not liable? For a discussion of "punitive damages" see *Alamo Nat'l Bank v. Kraus,* 616 S.W.2d 908, 910 (Tex. 1981) and TEX. CIV. PRAC. & REM. CODE §§ 41.001 *et seq.* (Vernon 1997).

Adding "**employees**" or "**agents**" to the list of Indemnified Persons may capture damages not otherwise awarded against the Indemnified Person in its capacity as employer. *See Fort Worth Elevators, Co. v. Russell,* 70 S.W.2d 397, 406 (Tex. 1934), *overruled on other grounds by Wright v. Gifford-Hill & Co.,* 725 S.W.2d 712 (Tex. 1987)-a corporation may be liable in punitive damages for gross negligence only if the corporation itself commits gross negligence. Because a corporation can "act only through agents of some character," *Fort Worth Elevators,* 70 S.W.2d 402, courts have developed tests for distinguishing between acts that are solely attributable to agents or employees and acts that are directly attributable to the corporation. *See Hammerly Oaks, Inc. v. Edwards,* 958 S.W.2d 387 (Tex. 1997). A corporation is liable for punitive damages if it authorizes or ratifies an agent's gross negligence or if it is grossly negligent in hiring an unfit agent; *See King v. McGuff,* 234 S.W.2d 403 (Tex. 1950)-adopting RESTATEMENT OF TORTS § 909; *Purvis v. Prattco, Inc.*, 595 S.W.2d 103, 104 (Tex. 1980)-citing the RESTATEMENT (SECOND) OF TORTS § 909, which is unchanged form the original RESTATEMENT OF TORTS § 909; or if it commits gross negligence through the acts or omissions of a "vice principal" *See Hammerly Oaks, Inc. v. Edwards,* 958 S.W.2d 387, 389 (Tex. 1997). A "vice principal" encompasses: (a) corporate officers; (b) those who have authority to employ, direct, and discharge servants of the master; (c) those engaged in the performance of nondelegable or absolute duties of the master; and (d) those to whom the master has confided the management of the whole or a department or a division of the business. *Hamerly Oaks,* 958 S.W.2d 391.

(6) Contractual Exceptions

(a) Broad Exception for Liabilities of Indemnified Person. In *Renfro Drug Co. v. Lewis*, 235 S.W.2d 609 (Tex. 1950), 23 A.L.R.2d 1114 (1950), the court refused to extend the lessee's indemnity covering injuries to persons occurring on the leased premises from any cause to include liabilities arising out of defects in the premises where the indemnity contained an exception for "any liability which lessor would be liable." *Also accord Port Royal.*

(b) Exceptions for Gross Negligence, Knowing Actions, and Willful Misconduct of Indemnified Person.

i) "Gross Negligence". Gross negligence is more than momentary thoughtlessness, inadvertence, or error of judgment. It means such an entire want of care as to establish that the act or omission was the result of actual conscious indifference to the rights, safety, or welfare of the person affected. TEX. CIV. PRAC. & REM. CODE ANN. § 41.001(5) (Vernon 1997). The test for gross negligence contains both an objective and a subjective component. *Transportation Ins. Co. v. Moriel,* 879 S.W.2d 10, 21, 22 (Tex. 1994). Objectively, the defendant's conduct must involve an extreme degree of risk, which is a function of both the magnitude and the probability of the anticipated injury to the plaintiff. *Also see Wal-Mart Stores, Inc. v. Alexander,* 878 S.W.2d 322, 325-26 (Tex. 1993). Subjectively, there must be evidence that the defendant had actual, subject awareness of the risk involved, but nevertheless was consciously indifferent to the extreme risk. The defendant knew about the peril, but its acts or omissions demonstrated that it did not care. *Moriel*, at 21; *Alexander* at 326; *Mobil Oil Corp. v. Ellender*, 968 S.W.2d 917, 922 (Tex. 1998). *Also see Universal Services Co., Inc. v. UNG,* 904 S.W.2d 638 (Tex. 1995) for a case arising under the common law definition of "gross negligence." The fact that a defendant exercises "some care" does not insulate the defendant from gross negligence liability. *See Moriel,* 879 S.W.2d at 20 (discussing cases before *Burk Royalty Co. v. Walls,* 616 S.W.2d 911, 921-22 (Tex. 1981) that erroneously focused on "entire want of care" part of the gross negligence definition in reasoning that "some care" defeated a gross negligence finding. In 1995 the Legislature substituted "malice" for gross negligence as the prerequisite for punitive damages. However, the Legislature also defined "malice" with a definition mirroring the definition of "gross negligence" in *Transportation Ins. Co. v. Moriel,* 879 S.W.2d 10, 23 (Tex. 1994). TEX. CIV. PRAC. & REM. CODE § 41.001(7) (Vernon 1997).

ii) A Continuum of Culpable Mental States. The court in *Kenneth H. Hughes Interests v. Westrup*, 879 S.W.2d 229, 232-33 (Tex. App.--Houston [1st Dist.] 1994, *writ denied*) interpreted an exclusion from a contractor's indemnity contained in a construction contract between a commercial landlord and its contractor for

> "any claim aris(ing) out of the sole and gross negligence or willful misconduct of Owner (the commercial landlord, the Indemnified Person)"

as including as an exclusion the landlord's "**knowing**" violation of the warranty of commercial habitability and/or "knowing deceptive trade practice" in its lease with the injured tenant.

This case involved a shoe store that was put out of business in the landlord's shopping center by repeated flooding arising out of the action of a backhoe operator

of a subcontractor of landlord's construction contractor. The case involved dual theories of recovery, the negligence of the contractor and the knowing deceptive trade practice and breach of warranty of the landlord.

The backhoe operator accidentally broke a sewer line, and covered it up after he discovered his error instead of reporting the accident. The tenant reported to the landlord that water was seeping from a leak in the slab outside of its premises. The landlord, who was unaware of the backhoe operator's actions, repeatedly reassured the tenant after each of several floods, that it had corrected the problem when, in fact, it knew it had not.

The court held that the intent of the parties by excluding gross negligence, also must have intended to exclude knowing conduct of the landlord, which is a "more culpable standard than gross negligence." The court noted that to hold otherwise would be to hold that the intent of the parties was that the indemnitees would not be entitled to indemnity for an act done with the mental state at the low end of the "continuum" of culpable mental states, but *would* be so entitled for an act done with a mental state that is higher on the scale, *i.e.,* an act that is *more* culpable than another for which they indisputably are not entitled to indemnity. *Luna v. North Star Dodge Sales, Inc.*, 667 S.W.2d 115, 118 (Tex. 1984).

iii) Exception for Sole Negligence Includes Sole Gross Negligence. The court in *Crown Central Petroleum Corp. v. Jennings*, 727 S.W.2d 739 (Tex. App.-- Houston [1st Dist.] 1987, *no writ*) held that a clause "excepting only claims arising out of accidents resulting from the sole negligence of Owner" included accidents arising from the sole gross negligence of the owner.

iv) Exception for Sole Negligence Does Not Affirmatively Create Indemnity for Indemnified Person's Concurrent Negligence. However, the court of appeals' reliance in *Crown Central Petroleum Corp. v. Jennings* upon its opinion in *Singleton v. Crown Central Petroleum Corp.*, 713 S.W.2d 115 (Tex. App.--Houston [1st Dist.] 1985) was misplaced since, after citing the *Singleton* writ history of "writ ref'd n.r.e," the Texas Supreme Court withdrew its opinion and reversed the court of appeals in *Singleton* at 729 S.W.2d 690 (Tex. 1987). The court of appeals both in *Jennings* and *Singleton* erroneously concluded that the above quoted language "excepting ..." was an express statement that the concurrent negligence of the Indemnified Person was indemnified by the Indemnifying Person. As noted in the discussion of the Texas Supreme Court cases construing *Ethyl*, the Texas Supreme Court held that this type language states what is not to be indemnified, and not what is indemnified.

(7) Scope of the Work Limitations. Courts have attempted to limit the scope of the Indemnified Matters to job site injuries or activities and work within the scope of the contract.

(a) Contemplated Work. Indemnified Liabilities may be contractually limited to such injuries as **"arise out of"** or are **"in connection with"** the work being performed by the Indemnifying Person. If the indemnity is so limited, then it might be held not to cover the negligent acts of the Indemnified Person that are unrelated to the performance of the scope of the work by the Indemnifying Person. *Sun Oil Co. v. Renshaw Well Serv., Inc.,* 571 S.W.2d 64, 70-71 (Tex. App.--Tyler 1978, *writ ref'd n.r.e.*); *Westinghouse Electric Corp. v. Childs-Bellows*, 352 S.W.2d 806, 832 (Tex. App.--Ft. Worth 1961, *writ ref'd*); and *Martin Wright Electric Co. v. W.R. Grimshaw Co.*, 419 F.2d 1381 (5th Cir. 1969), *cert. denied*, 397 U.S. 1022 (1970). The court in *Westinghouse Electric Corp. v. Childs-Bellows*, 352 S.W.2d 806 (Tex. Civ. App.--Ft. Worth 1961, *writ ref'd*) found that the indemnity agreement of a subcontractor did not include injuries to the subcontractor's employees who had been injured through the negligence of employees of the contractor engaged in work unrelated to the subcontract.

However, this result might also be explained as being an attempt by pre-*Ethyl* courts to limit indemnity agreements with the "clear and unequivocal" test. *See Dupre v. Penrod Drilling Corp.*, 993 F.2d 474, 479 (5th Cir. 1993).

In another case, the court held that the subcontractor's indemnity did not extend to the death of the subcontractor's employee caused by the negligent acts of the contractor's employees. *Brown & Root, Inc. v. Service Painting Co.*, 437 S.W.2d 630 (Tex. Civ. App.-- Beaumont 1969, *writ ref'd*). The death of the employee of the subcontractor did not "occur in connection with" the subcontracted work, notwithstanding the fact that the employee was engaged in sublet work at the time of the employee's death. The work being performed by the employee of the general contractor was not connected to the work being performed by the employee of the subcontractor. The *Brown & Root* indemnity clause reads:

> **Provision**: Subcontractor agrees to indemnify and to save General Contractor ... harmless from and against all claims ... which may be caused or alleged to have been caused in whole or in part by, or which may occur or be alleged to have occurred in connection with, the performance of the Sublet Work.

See also Westinghouse Electric Corp. v. Childs-Bellows, 352 S.W.2d 806 (Tex. Civ. App.--Ft. Worth 1961, *writ ref'd*); *Ohio Oil Co. v. Smith*, 365 S.W.2d 621 (Tex. 1963); *Spence & Howe Constr. Co. v. Gulf Oil Corp.*, 365 S.W.2d 631 (Tex. 1963); and *Alamo Lumber Co. v. Warren*, 316 F.2d 287 (5th Cir. 1963).

(b) Job Site. In *Sun Oil Co. v. Renshaw Well Service, Inc.*, 571 S.W.2d 64 (Tex. Civ. App.--Tyler 1978, *writ ref'd n.r.e.*), the court found that the indemnified person was not entitled to indemnification against injury to a worker injured while driving from the work site after completion of the work.

In *Martin Wright Electric Co. v. W. R. Grimshaw Co.*, 419 F.2d 1381 (5th Cir. 1969), *cert. denied* 397 U.S. 1022 (1970), the court refused to extend the subcontractor's indemnity to include the death of a subcontractor's employee killed while leaving work

after putting his tools away where the death was caused solely by the contractor's negligence.

(8) Contemplated Time Covered. Indemnity provisions have been strictly construed to limit the time of the occurrence of the Indemnified Matters.

In *Manges v. Willoughby*, 505 S.W.2d 379 (Tex. Civ. App.--San Antonio 1974, *writ ref'd n.r.e.*), the court construed an indemnity by a sublessee to the sublessor, which had "assumed all obligations" under the lease, as not covering damages to the leased premises which occurred prior to the sublease.

However, an indemnity provision whereby an equipment lessee agreed to indemnify the lessor for loss, damage, and expense incurred to the leased equipment and agreed to be responsible for the return of the leased equipment at its expense did not terminate when the equipment was delivered by the lessee to a third party selected by the lessee, but terminated when actually delivered back to the lessor. *M. M. Sundt Constr. Co. v. Contractors Equipment Co.*, 656 S.W.2d 643 (Tex. App.--El Paso 1983, *no writ*).

(9) Negligence of Indemnifying Persons Not Same as Negligence of Indemnified Persons. Clearly, provisions requiring the Indemnifying Persons to indemnify the Indemnified Persons against loss resulting from the negligent acts or omissions of the Indemnifying Persons do not cover loss caused by the negligence of the Indemnified Persons. *Humble Oil & Refining Co. v. Wilson*, 339 S.W.2d 954 (Tex. Civ. App.--Waco 1960, *writ ref'd n.r.e.*) and numerous other cases cited herein. Extensive litigation over the intent of the drafters of such indemnity clauses lead the Texas Supreme Court to adopt the "express negligence" doctrine discussed in **Article IIB - Contractual Indemnity - Indemnity Against One's Own Negligence** above.

F. Particular Provisions.

1. Attorney's Fees for Defense by Indemnified Person of Claim.

a. General Rule. The general rule is that attorney's fees are **not** recoverable by a claimant unless there is a statutory provision allowing attorney's fees.

b. Attorney's Fees in Common Law Indemnity Actions.

(1) Liability for Attorney's Fees in Defending Against Claims if Claim Not Settled; But No Liability for Attorney's Fees for suit to Collect on Common Law Indemnity. Attorney's fees incurred in suing to enforce a right to common indemnity are **not damages** recoverable in a common law indemnity action by the indemnitee against indemnitor. *See Conann Constructors, Inc. v. Muller*, 618 S.W.2d 564 (Tex. Civ. App.--Austin 1981, *writ ref'd n.r.e.*) where the court held that a breach of implied warranty of fitness gives rise to a common law action for indemnity for damages including damages to a third party (homeowner damaged by overflowing septic tank sued neighbor who sought indemnity from contractor).

The court held that common law indemnity includes **attorney's fees in defending the liability suit but does not include the attorney's fees in suing the contractor seeking indemnity**. *Central Consolidated, Inc. v. Robertshaw Controls Co.*, 868 S.W.2d 910 (Tex. App.--Beaumont 1994, *no writ*)--innocent retailer may seek indemnity from manufacturer for its attorney's fees incurred in establishing that the retailer was merely an "innocent conduit."

(2) DTPA and Common Law Liability for Attorney's Fees. TEX. BUS. & COMM. CODE ANN. § 17.555 (Vernon 1987), the Texas Deceptive Trade Practices Act provides that a party is "indemnified" for all sums it is required to pay as a result of defending an action brought against it under the DTPA, including costs and attorney's fees. Section 17.555 provides

> A person against whom an action has been brought under this subChapter may seek *contribution or indemnity* from one who, under the statute law or at common law, may have liability for the damaging event of which the consumer complains. A person seeking indemnity as provided by this Section may recover all sums that he is required to pay as a result of the action, his *attorney's fees* reasonable in relation to the amount of work performed in maintaining his action for indemnity, and his costs.

(a) No Liability for Common Law Indemnified Person's Attorney's Fees in Defending Plaintiff's DTPA Claim Absent Liability to the Plaintiff by the Common Law Indemnifying Person. The DTPA does not describe the nature of or set the standard for obtaining the statutory rights to contribution and indemnity. The Texas Supreme Court in *Plas-Tex, Inc. v. U.S. Steel Corp.*, 772 S.W.2d 442, 446 (Tex. 1989) concluded that this Section of the DTPA was "intended to incorporate existing principles of contribution and indemnity law into DTPA cases" as opposed to creating independent statutory rights to indemnity. Therefore, in *Plas-Tex* the supreme court reversed the trial court's award to a defendant (a product seller) against another defendant (the product manufacturer) for its attorney's fees the product seller incurred in successfully defending a consumer's DTPA action. The consumer, a buyer of resins used in the manufacture of fiber glass pools, brought a DTPA action against the resin manufacturer and the seller.

Since the court of appeals had reversed the trial court's finding that the product manufacturer was liable for the event complained of by the plaintiff, the supreme court held that the product manufacturer had no obligation of indemnity to the product seller, including the product seller's attorney's fees in successfully defending the suit. "There is no right of indemnity against a defendant who is not liable to the plaintiff." *Plas-Tex* at 446 *citing Hunter v. Ft. Worth Capital Corp.*, 620 S.W.2d 547, 553 (Tex. 1981); *Brown & Root, Inc. v. Rust Eng'g*, 679 S.W.2d 576, 578 (Tex. App.--Texarkana 1984, *writ ref'd n.r.e.*).

(b) Liability by Common Law Indemnifying Person for Common Law Indemnified Person's Attorney's Fees in Defending Plaintiff's DTPA Claim, if Common Law Indemnifying Person

Liable to the Plaintiff. In *Swafford v. View-Caps Water Supply Corp.,* 617 S.W.2d 674 (Tex. 1981), the indemnitor, View-Caps, was found to be liable to the plaintiff, but the indemnitees, Swafford and Baker, were absolved of liability. In sustaining attorney's fees to the indemnitees, the Texas Supreme Court said

> The only question before this Court is whether Swafford and Baker are entitled to indemnity from View-Caps for their attorney fees under Section 17.55A of the DTPA (predecessor Section to 17.555A). We hold that Swafford and Baker are entitled to recover attorney's fees under the express provisions of the statute. ... *The jury found that View-Caps was liable for the event complained of by Purcell.* The statute expressly authorizes indemnity for attorney's fees in this situation.

(3) No Attorney's Fees for Indemnified Person's Defense, if Indemnifying Person Settles Plaintiff's Claim. It has been held that **settlement** of the claim by the indemnitor, which if proved would establish a common law right of indemnification, **eliminates attorney's fees** incurred by the indemnitee in defending suit. In *Humana Hospital Corp. v. American Medical Systems, Inc*., 785 S.W.2d 144 (Tex. 1990), the Texas Supreme Court considered a question certified by the United States Court of Appeals. The court was asked:

> Under Texas law, is a seller of a product entitled to indemnification from the manufacturer for attorney's fees incurred by seller during the litigation where the manufacturer settles the case with the plaintiff before a judicial determination of the liability of the parties is made?

Id. at 145.

Plaintiff had brought a negligence/strict products liability suit to recover damages arising from the rupture of a prosthetic penile device. The device was designed, manufactured and sold by American Medical Systems to Humana Hospital. Humana Hospital supplied the device to plaintiff's physician for surgical implant. Humana filed a motion for summary judgment seeking indemnity and attorney's fees from American Medical Systems. The motion was granted, entitling the hospital to be indemnified by American Medical Systems if the plaintiff recovered against Humana. American Medical settled the suit with the plaintiff without any judicial determination of the liability of the parties. Humana objected to the court's order disposing of the case because the court did not award Humana the attorney's fees it had incurred in defending the case.

Quoting its holding in *Plas-Tex*, the Texas Supreme Court in *Humana Hospital* held that there is **no** right of indemnity against a defendant who is not liable to the plaintiff. Since the settlement did not include a court determination that American Medical was negligent or that the prosthesis was unreasonably dangerous, Humana could not obtain indemnity for its defense costs.

Although this holding appears to be based on common law indemnity, it may also be applicable to contractual indemnity claims. *See McDaniel v. Anheuser-Busch, Inc.,* 987 F.2d 298 (5th Cir. 1993) holding the indemnitor was not obligated to defend the indemnitee against all claims and suits, or for costs incurred in defense of baseless claims, since the indemnity clause required only that the indemnitor indemnify for injuries "caused" by acts or omissions of the indemnitee.

c. Contractual Indemnity Covering "Attorney's Fees" and "Costs" as an Exception. Attorney's fees have been recoverable by the Indemnified Person against the Indemnifying Person in certain contractual indemnity cases.

(1) Attorney's Fees in Defending Against a Claim and Enforcing Indemnity as Indemnified Liabilities. The expense of defending a liability suit and in subsequently enforcing the contractual indemnity are reimbursable when the Indemnified Person recovers contractual indemnification from the Indemnifying Person. An Indemnified Person's attorney's fees in defending a liability suit are recoverable from the Indemnifying Person as "indemnified damages" even though not expressly mentioned in the indemnity provision. Attorney's fees may be awarded to the Indemnified Person pursuant to TEX. CIV. PRAC. & REM. CODE § 38.001(8) (Vernon 1997) in connection with a suit against the Indemnifying Person for its breach of its contract of indemnity. *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*). The purpose of indemnification is to make the Indemnified Person whole. *Tubb v. Bartlett,* 862 S.W.2d 740, 751 (Tex. App.--El Paso 1988, *writ denied*); *Continental Steel Co. v. H. A. Lott, Inc.,* 772 S.W.2d 513, 517 (Tex.App.-Dallas 1989, *writ denied*); *Texas Const. Assoc., Inc. v. Balli*, 558 S.W.2d 513 (Tex. Civ. App.--Corpus Christi 1977, *no writ*); *Fisher Constr. Co. v. Riggs*, 320 S.W.2d 200 (Tex. Civ. App.--Houston 1959), *rev'd on other grounds*, 325 S.W.2d 126 (1959) *and vacated on other grounds*, 326 S.W.2d 915 (Tex. Civ. App.--Houston 1959); *Barnes v. Calgon Corp.,* 872 F. Supp. 349, 353 (E.D. Tex. 1994).

However, a different rule may apply to "costs" and "expenses" beyond attorney's fees. In *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*) the court held that failure of the indemnity provision to expressly cover the Indemnified Person's litigation costs prevented recovery of the following expenses incurred by its attorney: filing fees, courier fees, postage, telephone expenses, long distance charges, and fax charges. The court considered these costs to be included within the hourly billing rates and reasonable fees of the attorney, unless the indemnity contract expressly covered these items as an Indemnified Matter.

(2) No Attorney's Fees for Indemnified Person's Defense of Negligence Claim if Indemnity Fails Express Negligence Test. The Texas Supreme Court in *Fisk Electric Co. v. Constructors & Assoc.s, Inc.*, 888 S.W.2d 813 (Tex. 1994) held that there is no obligation to indemnify an Indemnified Person for its costs, including any attorney's fees it incurs, resulting from a claim made against it for its own negligence unless the indemnification agreement meets the express negligence test. It is undisputed that the indemnity provision did not expressly provide that the

Indemnifying Person, Fisk Electric Co., agreed to indemnify Constructors for Constructor's negligence.

The court of appeals had held that an obligation to indemnify one for its attorney's fees and costs of defense is separate from an obligation to indemnify one for its own negligence. Consequently, the court of appeals concluded that in order to obtain summary judgment, thus avoiding liability under the indemnity agreement for the Indemnified Person's cost of defense, the Indemnifying Person, Fisk Electric Co., had to first establish that the Indemnified Person, Constructors, was negligent.

This case arose when an employee of Fisk, a subcontractor, sued Constructors, the general contractor, for injuries the employee sustained in performing electrical work at One Shell Plaza. Constructors brought a third-party action against Fisk seeking contractual indemnity.

The indemnity clause provided indemnity for the following liabilities:

Provision:

> 11.3 INDEMNIFICATION AND HOLD HARMLESS CLAUSE: To the fullest extent permitted by law, (Fisk) shall indemnify, hold harmless, and defend (Constructors) ... from and against all claims, damages losses, and expenses, including but not limited to attorney's fees, arising out of or resulting from the performance of (Fisk's) work ... provided that any such claim, damage, loss, or expense (a) is attributable to bodily or personal injury, sickness, disease, or death, or patent infringement, or to injury ... and (b) is caused in whole or in part by any negligent act or omission or any act or omission resulting in the strict liability of (Fisk) or anyone directly or indirectly employed by it(,) anyone for whose acts it may be liable, or is caused by or arises out of any products, material, or equipment furnished by (Fisk).....

The court of appeals concluded that the summary judgment proof offered by Fisk only established that the plaintiff claimed Constructors was negligent and that the indemnity provision did not expressly state that Fisk would indemnify Constructors from its own negligence.

The supreme court noted that following *Ethyl*, there existed a split of authorities among the courts of appeal.

The court of appeals in *Fisk* relied on the following post-*Ethyl* court of appeals' decisions allowing recovery of defense costs: *Construction Investments and Consultants, Inc. v. Dresser Industries, Inc.* 776 S.W.2d 790, 792 (Tex. App.–Houston [1st Dist.] 1989, *writ denied*); *Continental Steel Co. v. H.A. Lott, Inc.,* 772 S.W.2d 513 (Tex. App.--Dallas 1989, *writ denied*); *M.M. Sundt Const. Co. v. Contractors Equipment Co.*, 656 S.W.2d 643 (Tex. App.--El Paso 1983, *no writ*); *Copeland Well Service, Inc. v. Shell Oil Co.,* 528 S.W.2d 317 (Tex. App.--Tyler 1975, *writ dism'd*); *R. L. Jones Co. v. City of San Antonio,* 809 S.W.2d 565, 569 (Tex. App.--San Antonio 1991, *no writ*); *R.B. Tractors, Inc. v. Mann,* 800 S.W.2d 955 (Tex. App.--San Antonio 1990, *no writ*); a Fifth Circuit opinion: *Patch v. Amoco Co.*, 845 F.2d 571 (5th Cir. 1988); *Champlin Petroleum Co. v. Goldston Co.,* 797 S.W.2d 165, 166 (Tex. App.--Corpus Christi 1990, *writ denied*); and a pre-*Ethyl* Texas Supreme Court opinion: *Cira & Payne, Inc. v. Wallace & Riddle,* 484 S.W.2d 559, 562 (Tex. 1972).

However, the supreme court found that the express negligence requirement for the enforcement of an indemnity agreement is not an affirmative defense to be alleged and proved by the defendant Indemnifying Person, but rather is a rule of contract construction. The court held that Fisk's obligation to pay attorney's fees arose out of its duty to indemnify. Absent a duty to indemnify, there is no obligation to pay attorney's fees.

Additionally, the court cited cases from other jurisdictions drawing a parallel to the indemnity contract of a commercial general liability policy. As noted by the dissent in *Continental Steel*, in this respect, the indemnity provision operates like an insurance policy; if an insurance policy excludes coverage for intentional torts, an insured cannot claim coverage for fees and costs even if it successfully defends against allegations that it committed an intentional tort. *See Continental Steel,* 772 S.W.2d at 523 (Lagarde, J. dissenting).

The supreme court observed that a rule like that proposed by Constructors regarding defense expenses would

> "leave indemnitors liable for a cost resulting from a claim of negligence which they did not agree to bear. Significantly, it would also leave indemnitors vulnerable to indemnitees who might settle cases without admitting negligence, leaving the indemnitor to pay the costs of settlement and defense."

The supreme court declined to carve out an exception to the express negligence rule for contracts which although they did not expressly indemnify the Indemnified Person for its own negligence, clearly, expressly or broadly covered the Indemnified Person's defense costs. In this regard, the supreme court was unwilling to follow the contract interpretation used by Chief Justice Tom Phillips, when Chief Justice Phillips was the trial court judge in *Construction Investments and Consultants, Inc. v. Dresser Industries, Inc.*, 776 S.W.2d 790, 792 (Tex. App.--Houston [1st Dist.] 1989, *writ denied*).

The Fisk indemnity language appears to be patterned on the indemnity clause contained in the AIA A401 Standard Form of Agreement Between Contractor and Subcontractor (1987 Edition). Does the AIA form pass the express negligence test? Is its indemnity provision conspicuous? *See* Appendix 1.

Also see Glendale Construction Services, Inc. v. Accurate Air Systems, Inc., 902 S.W.2d 536 (Tex. App.--Houston [1st Dist.] 1995, *writ denied*), holding no right to attorney's fees absent an enforceable indemnity provision.

In the *Dresser* case, the court of appeals found the following extensive contract language as *clearly indicating the intent* of the Indemnifying Person to cover the Indemnified Person's attorney's fees

($142,633.20) where the Indemnified Person successfully defended against the negligence suit, even though the indemnity provision otherwise would not pass the express negligence test:

Provision:

> Contractor (CIC) shall, except as otherwise expressly provided herein, indemnify, protect and save Dresser ... harmless against any and all actions ... including *costs of litigation, attorney fees and reasonable expenses in connection therewith* ... whether or not such loss, injury, or damage shall be valid or groundless, and Contractor agrees that in case Dresser ... shall be made defendant in any suit ..., *Contractor*, immediately upon notice from Dresser, *shall be bound and obligated to assume the defense thereof, including the settlement negotiations and shall pay* ... expenses resulting from ... . *It is understood and agreed by Contractor that in case Dresser is made defendant in any suit or action and Contractor fails or neglects to assume the defense thereof, after having been notified so to do by Dresser, that Dresser may compromise and settle or defend any such suit or action, and Contractor shall be bound and obligated to reimburse Dresser for the amount expended by it in settling and compromising any such claim, or in the amount expended by Dresser in paying any judgment rendered therein, together with all reasonable attorneys' fees incurred by Dresser by reason of its defense or settlement of such claims*. (Emphasis added by court.)

Id. at 791.

The court of appeals held that CIC's obligation to indemnify Constructors for attorney's fees and costs in the defense of the underlying suit is separate from CIC's obligation to indemnify Constructors for Constructors' negligence. The court held that "an Indemnified Person may recover attorney's fees and costs where it was not found negligent, even though the indemnity provision did not meet the express negligence standard."

2. Choice of Laws.

a. No Express Choice of Laws Provision. In *Maxus Exploration Co., f/k/a Diamond Shamrock Exploration Co. v. Moran Bros., Inc*., 817 S.W.2d 50 (Tex. 1991), the Texas Supreme Court had to determine whether Kansas law or Texas law applied absent an express choice of laws provision in a contract containing indemnity provisions. In *Maxus*, the Texas Supreme Court determined that the laws of Kansas were to be applied to the indemnity clause to determine if it was enforceable. The indemnity clause involved in *Maxus* is the mutual indemnity clause contained in the standard form "Daywork Drilling Contract" published by the International Association of Drilling Contractors.

The oil well operator (Maxus Exploration f/k/a Diamond Shamrock) brought a declaratory judgment action in Texas against the drilling contractor (Moran Bros.) to determine the validity of the contractual indemnity provision contained in the Drilling Contract. Diamond Shamrock had previously in response to the demand of Moran Bros. accepted the defense of an injury claim filed by an employee of one of Diamond Shamrock's contractors (Boydstun). Moran Bros. and Maxus agreed to reserve for determination in a subsequent suit the issue of the enforceability of the indemnity provision.

The employee of the contractor of Diamond was injured while working on Moran's rig. The accident occurred in Kansas where Moran Bros. was performing contract drilling services for Maxus. The employee, a resident of Oklahoma, sued Moran, a Texas corporation, in the United States District Court in Kansas. Moran filed a cross- action against Diamond Shamrock for indemnity under the drilling contract. Diamond Shamrock undertook to defend Moran in the litigation. Moran Bros. and Diamond Shamrock each reserved any right it might have to seek indemnity or other damages from the other. Based upon a jury verdict that Boydstun had suffered $3 million in damages caused 90% by Moran's negligence, the court rendered judgment against Moran for $2.7 million. Moran then settled with Boydstun. Diamond Shamrock and its insurer paid approximately half the settlement amount and Moran paid the balance. The supreme court followed the following steps in determining that Kansas law applied. The court stated

> In deciding which state's law should govern the construction of contractual rights we have previously looked to the principles stated in the RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971) [hereinafter the "Restatement"]. *DeSantis v. Wackenhut Corp*., 793 S.W.2d 670, 679 (Tex. 1990), *cert. denied*, 498 U.S. 1048, 111 S. Ct. 755, 112 L. Ed. 2d 775 (1991); *Duncan v. Cessna Aircraft Co*., 665 S.W.2d 414, 420 (Tex. 1984). We look to those principles again here.

Id. at 53.

In *Duncan v. Cessna Aircraft Co*., the Texas Supreme Court had to determine whether Texas or New Mexico law controlled the construction of a release executed by Duncan (on behalf of herself as widow and her minor children in a wrongful death action) in favor of Air Plains West, Inc. The Texas Supreme Court held that Texas had the most significant relationship to this issue. The court held that the release language which released Air Plains and "any other corporations or persons whomsoever responsible therefor, whether named herein or not" did not release Cessna, the manufacturer of the airplane. *Id*. at 418. The court assumed that the release would be enforceable under New Mexico law, but determined that since Texas had the most significant relationship to the matter, that Texas law would apply to construe the release. The court refused to be bound by the traditional tort choice of laws rule of *lex loci delecti* (*i.e*., apply the law of the place where the wrong occurred--New Mexico where the crash occurred). Similarly, the court noted that it would not follow other *lex loci* rules such as *lex loci contractus*.

> Consequently, the *lex loci* rules will no longer be used in this state to resolve conflicts problems. Instead, in all choice of law cases, except those contract cases in which the parties have agreed to a valid choice of law clause, the law of the state with the most significant relationship to the particular

> substantive issue will be applied to resolve that issue. (Italics added by author.)

Id. at 421.

(1) General Rule: In Absence of Choice of Laws Provision, Apply Law of State with Most Significant Relationship. The supreme court in *Maxus* referred to the following statement in the Restatement as controlling the determination of the appropriate state's laws to govern an indemnity in contracts containing no choice of laws provision:

> The existence of a contractual right to indemnity, and the rights created thereby, are determined by the law selected by application of the rules of §§ 187-188.

RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 173, Comment b (1971).

The Restatement sets forth the following general rule in Restatement § 188(1) to be applied in cases where the parties have not themselves chosen what law governs their agreement:

> The rights and duties of the parties with respect to an issue in contract are determined by the local law of the state which, with respect to that issue, has the **most significant relationship** to the transaction and the parties under the principles stated in § 6.

Section 188(2) lists the contacts comprising the relationship between transactions and locale ordinarily to be taken into account in applying the principles in § 6. These include:

(a) the place of contracting,
(b) the place of negotiation,
(c) **the place of performance**,
(d) the location of the subject matter of the contract, and
(e) the domicile, residence, nationality, place of incorporation and place of business of the parties.

(2) Law of Place of Performance Applicable to Service Contracts. The court, quoting *DeSantis*, found that as to service contracts "[a]s a rule, (the fact that the services are almost entirely in a particular state) that factor alone is conclusive in determining what state's law is to apply." *DeSantis v. Wackenhut Corp*., 793 S.W.2d at 679 (Tex. 1990). Section 196 of the Restatement states

> The validity of a contract for the rendition of services and the rights created thereby are determined, in the absence of an effective choice of law by the parties, *by the local law of the state where the contract requires that the services*, be rendered, *unless, with respect to the particular issue, some other state has a more significant relationship under the principles stated in § 6* to the transaction and the parties, in which event the local law of the other state will be applied.

(3) On Balance This Indemnity Contract Governed by Law Applicable to Contract Which Contains the Indemnity Provision. The court determined the law of Kansas, exclusive of its choice of laws rules, would be applied to the indemnity provision. Under Kansas law the indemnity provision was held by the Texas Supreme Court to be enforceable. The court followed the following analysis:

(a) Restatement Rule on Particular Contracts. The court noted that in some instances, it is more appropriate to consider the disputed contractual issue separately from the contract as a whole. RESTATEMENT (SECOND) OF CONFLICT OF LAWS Title C, Particular Issues, at 631-32 (1971) states

> ... most issues involving a contract will usually be governed by a single law, (occasionally) an approach directed to the particular issue, rather than to the kind of contract involved, will provide a more helpful basis for the decision of a choice-of-law question.

The court noted that even assuming that the indemnity obligations should be considered separately from the contract as to the determination of the applicable state rules, the indemnity obligations were performable for the most part in Kansas. Therefore, pursuant to § 196 relating to conflicts of laws in service contracts, the court determined that the law of the state of Kansas was to be used, unless some other state (Texas) had a more significant relationship to the transaction and the parties under the principles in § 6 of the Restatement.

(b) Determination if Another State Has a More Significant Relationship than State of Performance. Section 6 provides that absent a statutory directive concerning the law to be applied in a case, the following seven factors are relevant:

> the factors relevant to the choice of the applicable rule of law include
>
> 1) the needs of the interstate and international systems,
> 2) the relevant policies of the forum,
> 3) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue,
> 4) the protection of justified expectations,
> 5) the basic policies underlying the particular field of law,
> 6) certainty, predictability and uniformity of result, and
> 7) ease in the determination and application of the law to be applied.

i) Public Policies of Both States Examined. The court first examined the *public policies of both states* to determine if either state's laws would declare the particular indemnity provision to be unenforceable as a matter of law.

a) Texas. The court noted two expressions of Texas public policy relating to the indemnity provisions.

i) Express Negligence. The court reviewed the language of the indemnity and

found that the language "without limit and without regard to the cause or causes thereof or the negligence of any party or parties" **met the express negligence test** applied in Texas. Citing identical language in *Theriot v. Bay Drilling Corp.*, 783 F.2d 527, 539-41 (5th Cir. 1986).

ii) Texas Oilfield Anti-Indemnity Statute. After reviewing arguments that the indemnity provision was violative of the requirements for a valid indemnity provision under the Texas Oilfield Anti-Indemnity Statute, the court concluded that it was the Texas Legislature's intent only to protect Texas contractors who work on mineral wells and mines in Texas and not to read the statute to have an extraterritorial reach, absent some agreement between the parties. *Maxus* at 57. *See* TEX. CIV. PRAC. & REM. CODE ANN. § 127.002(a).

b) Kansas. The court noted that Kansas does not have an anti-indemnity statute and follows the "clear and unequivocal" test in enforcing indemnity provisions. The court concluded that the indemnity clause would meet the "clear and unequivocal" test under Kansas law.

ii) Remaining Six Factors Examined. Of the seven choice of laws principles in Section 6 of the Restatement, the court found that the following four factors militated clearly in favor of applying Kansas law: a) the protection of justified expectations; b) certainty, predictability and uniformity of result; c) ease in the determination and application of the law to be applied; and d) the basic policies underlying the particular field of law. The court analyzed these factors as follows:

> Although the parties did not express a choice of what state's law would govern their agreement, they should have expected that Kansas law would at least be invoked. Kansas law was in fact applied in Boydstun's personal injury action. Although a state may have an interest in applying its law to a particular issue arising under a contract, in circumstances like these it is less desirable that Kansas law govern Boydstun's action and Texas law govern the defendants' cross-claims than it is that the same law govern both.

Id. at 57.

As to the two remaining principles to be considered--the relevant policies of Texas and Kansas and the relative interests of each in determining the validity of indemnity agreements like the one before the court--the court found that each principle pointed to choosing a different state's law. The court declined to express its opinion on whether the particular provision in *Maxus* would violate the Texas Oilfield Anti-Indemnity Statute, assuming Texas law applied. Since the court concluded that the Texas statute was not designed to have extraterritorial reach and Kansas had no public policy against such indemnity provisions, the court held that on balance the factors required the application of Kansas law.

b. Express Choice of Laws Provision. The Texas Supreme Court has adopted the principles set forth in § 187 of the RESTATEMENT (SECOND) OF CONFLICT OF LAWS (1971) in order to determine if a choice of laws provision is to be enforced. *DeSantis v. Wackenhut Corp*., 793 S.W.2d 670 (Tex. 1990). *See* Weiner and Ale, *Making Choice of Law a Contact Sport: Contractual Choices of Law in Texas*, 54 TEX. B.J. 262 (Mar. 1991) for an analysis of the *DeSantis* opinion and for suggestions for maximizing the chance that a contractual choice of laws provision will be enforced by a Texas court. If the law of another state is chosen and the contract is for the sale, lease, exchange, or other disposition of goods for the price, rental, or consideration of $50,000 or less, any element of the execution of the contract occurred in Texas and a party is a resident of Texas or is an entity created under the laws of Texas, then the boldface type, capital letters, or other conspicuous manner requirements of TEX. BUS. & COMM. CODE ANN. § 35.52 (Vernon Supp. Pamphlet 2003) will apply.

Under the Restatement rule, the choice of laws provision will be upheld unless all the factors in Restatement § 187(2)(b) are met; namely, (a) some other state's law would apply had the parties not made a choice; (b) that other state has a materially greater interest than does the chosen state in the enforceability of the contractual provisions at issue; and (c) the contractual provisions at issue violates a fundamental policy of that other state.

New Mexico has upheld a provision choosing Texas law to apply to an indemnity that indemnified against the Indemnified Person's negligence, even though such an indemnity would not be enforceable under New Mexico law. The New Mexico court found that the provision did not violate a fundamental public policy of the State of New Mexico even though New Mexico statutes prohibited a similar contractual indemnity for contracts governed by New Mexico law. The court found that the same public policy could be upheld (promotion of safety) by upholding the indemnity since the Indemnifying Party also was required to obtain insurance supporting its indemnity. *Regan v. McGee Drilling Corp.,* 933 P.2d 867 (New. Mex. 1997) ("it is said that courts should invoke this public policy exception only in 'extremely limited' circumstances.... Otherwise, since every law is an expression of a state's public policy, the forum law would always prevail unless the foreign law were identical, and the exception would swallow the rule (rule-the rights of the parties to a contract are primarily determined by the terms of the contract.)."

3. Assignability. The ability to assign an indemnity or to include within the scope of an indemnity subsequent property owners is a valuable right that can add value to a property. A typical contract containing an indemnity may contain a standard "successor and assign" provision. Consideration should be given to whether this provision extends to the indemnity obligation. For example, an environmental indemnity from a major oil company in connection with the sale of the company's decommissioned oil refinery can be like an insurance policy against otherwise uninsurable environmental risks.

4. Cumulative or Exclusive Remedy. The indemnity should address whether its rights are exclusive of any other remedy available to the

Indemnified Person. It might be argued that an indemnity was intended to be the exclusive remedy afforded to the Indemnified Person as to a particular risk. The wording of the indemnity will be strictly construed and might not cover a subsequently occurring risk, unless expressly covered (*e.g.,* change of law or change in classification of a substance to a hazardous substance in the case of an environmental indemnity).

5. Powers Granted to Indemnified Person. The following types of provisions granting broad powers to an Indemnified Person have been upheld.

a. Modification of Instruments Increasing Liability. It has been held that an indemnity contract is not contrary to public policy even though the contract makes vouchers or affidavits *prima facie* evidence of any loss paid by the Indemnified Person and gives the Indemnified Person power to alter and modify instruments and to execute new obligations that fix the Indemnifying Person's liability without notice to the Indemnifying Person.

In *Hammond v. Travelers Indem. Co.*, 553 S.W.2d 205 (Tex. Civ. App.--Houston [14th Dist.] 1977, *no writ*), the court upheld a clause in an indemnification agreement in a surety bond which provided for indemnification of all claims resulting from suretyship, or any renewal, extension, modification, or continuation for suretyship or additional suretyship even though increases in the surety bond were made without the knowledge or consent of the Indemnifying Person (the surety company).

b. Expenses Incurred in Good Faith. A provision requiring the Indemnifying Person (principal on a surety bond) to reimburse the Indemnified Person for all disbursements made by it in good faith, belief of liability, necessity, or expediency, regardless of whether such factors existed in actuality, has been upheld. *Central Surety & Ins. Corp. v. Martin*, 224 S.W.2d 773 (Tex. Civ. App.--Beaumont 1949, *writ ref'd*); *Shaw v. Massachusetts Bonding & Ins. Co.*, 373 S.W.2d 553 (Tex. Civ. App.--Dallas 1963, *no writ*).

c. Prior Notice Provision. In a case involving a lease which provided that a landlord's duty to repair the leased premises was conditioned upon the tenant giving notice or upon the landlord obtaining knowledge of the defect, the tenant was not entitled to indemnification from the landlord for liability for injuries sustained by the tenant's customer occasioned by an unreported defect in the premises. *Stool v. J. C. Penney Co.*, 404 F.2d 562 (5th Cir. 1968).

d. Discretion.

(1) No Common Law Indemnity for Voluntary Settlements of Indemnified Liability. Settlement by one joint tortfeasor extinguishes any common law and statutory contribution rights such person may have had. *Beech Aircraft Corp. v. Jinkins,* 739 S.W.2d 19 (Tex. 1987); *International Proteins Corp. v. Ralston- Purina Co.,* 744 S.W.2d 932 (Tex. 1988); TEX. CIV. PRAC. & REM. CODE ANN. § 33.015(d) (Vernon 1997).

In *MAN GHH Logistics GMBH v. Emscor, Inc.,* 858 S.W.2d 41 (Tex. App.–Houston [14th Dist.] 1993, *no writ*), the court of appeals denied both the seller and the buyer of a crane contribution and indemnity against the other after each had separately settled with the claimants for $3,000,000 for deaths and injuries sustained when a 152 foot tower crane fell over while being dismantled. The seller of the crane (Emscor) voluntarily settled two death claims in October, 1990. In November, 1990, the buyer of the crane (MAN GHH) agreed to a $3,000,000 judgment in favor of the two families.

Additionally, the court denied both the seller and the buyer respectively any right to "contractual contribution" pursuant to the reciprocal indemnity agreements contained in the Asset Purchase Agreement between seller and buyer. The Asset Purchase Agreement provided as follows:

Provision:

Indemnifications

Indemnification by Sellers. Sellers (Emscor), jointly and severally, hereby indemnify and hold harmless the Purchaser and its respective successors and assigns from and against any loss, damage, or expense (including reasonable attorney's fees) caused by or arising out of:

(i) any breach or default in the performance by Sellers of any covenant or agreement of Sellers contained in this Agreement;

(ii) any breach of warranty or inaccurate or erroneous representation made by Sellers herein, in any Exhibit hereto, or in any certificate or other instrument delivered by or on behalf of Sellers pursuant hereto;

(iii) third party claims regarding Emscor's management of Purchaser's Wolff tower cranes prior to the Closing Date;

(iv) third party claims regarding any matter relating to title to or Emscor's maintenance of the Purchase Assets prior to the Closing Date; or

(v) any liability arising out of any and all actions, suits, proceedings, claims, demands, judgments, costs, and expenses (including reasonable legal and accounting fees) incident to any of the foregoing.

The court dismissed each party's request for contractual indemnity and/or contribution from the other party. The court found that the quoted provision did not protect the buyer (and conversely the reciprocal provision did not protect the seller) because (1) it did not provide that the other party would reimburse the settling party for any voluntary settlements made with any plaintiffs; (2) the provisions did not mention "contribution" and failed to discuss any apportionment of fault; and (3) the provision did not express any intent by the parties for a claim for reimbursement. *Id.* at 43.

(2) No Equitable Right to Settle Indemnified Claim Absent Contractual Right to Settle Without Consent. In *Liberty Steel Co. v. Guardian Title Co. of Houston, Inc.*, 713 S.W.2d 358,

360 (Tex. App.--Dallas 1986, *no writ*), the court held there did not exist an equitable right in the Indemnified Party (Guardian Title Co.) to settle a claim (an abstract of judgment bonded around) when the Indemnifying Person did not voluntarily step in and assume the defense against the adverse claimant. The Indemnified Person had sent a letter to the Indemnifying Person requesting the Indemnifying Person to "honor the terms" of the indemnity agreement. The court found that the indemnity contract did not contain a provision obligating the Indemnified Person to offer to undertake the defense of the claim and that the Indemnifying Person never made a "tender of the defense" to the Indemnified Person. Therefore, the Indemnified Person could not obtain reimbursement of the amount paid to settle the adverse claim when the Indemnified Person settled the claim in violation of the following contractual provision:

Provision:

> no payment, compromise, settlement, accord or satisfaction shall be made without the prior written approval of Liberty Steel (the Indemnifying Person)....

(3) Settlement Authority. Delegating settlement authority to the Indemnified Person has been upheld.

Drafting: The indemnity provision attached in **Appendix 2 and 7** contains the following provision protective of the Indemnified Person in the conduct of the defense of an Indemnified Liability:

> (1) the Indemnified Person is permitted to employ its own counsel in addition to the counsel employed by the Indemnifying Person;
>
> (2) the cost of the Indemnified Person's counsel is also an Indemnified Liability;
>
> (3) the Indemnified Person is given the Sright to settle claims in the event that the Indemnifying Person does not provide a defense to the claim; and
>
> (4) amounts paid by the Indemnifying Person under such circumstances is an Indemnified Liability.
>
> *Also see* **Appendix 7 (Supplemental Provisions)** which sets out procedures for the Indemnified Person to determine if the Indemnifying Person will honor its obligation to provide a defense and, if not, for the Indemnified Person to employ counsel to defend the claim.

(a) Contracts. A court has upheld a provision in a contract that authorized a right-of-way owner to compromise and settle all claims for damage within the right-of-way in connection with an indemnity provision with a contractor. *Phillips Pipeline Co. v. McKown*, 580 S.W.2d 435 (Tex. Civ. App.--Tyler 1979, *writ ref'd n.r.e.*). *Also see Sieber & Calicutt, Inc. v. La Gloria,* ___ S.W.2d ___ 12-00-001-00123-CV (Tex.App.-Tyler 2001, *no writ*) and *Amerada Hess Corp. v. Wood Group Production Technology,* 30 S.W.3d 5 (Tex. App. [14th Dist.] 2000, *writ denied*) upholding settlement authority granted by an Indemnifying Person to an Indemnified Person.

(b) Bonds. An indemnity provision that "any decision, determination, settlement, defense, compromise, or other action in connection with any matter arising under an indemnity bond would be final, conclusive, and unconditionally binding on the indemnitor" has been upheld as not being against public policy. *Engbrock v. Federal Ins. Co.*, 370 F.2d 784 (5th Cir. 1967). In *Ford v. Aetna Ins. Co.*, 394 S.W.2d 693 (Tex. Civ. App.-- Corpus Christi 1965, *writ ref'd n.r.e.*), the court upheld an indemnity provision which granted the indemnified person (surety on a performance and payment bond) exclusive power to make conclusive determinations of claims and demands to be paid.

(4) Settlement Standards.

(a) Reasonable and Prudent. For a settling Indemnified Person to recover an amount of the settlement from this Indemnifying Person, the Indemnified Person must show the potential liability to a claimant and that the settlement was reasonable, prudent and made in good faith under the circumstances. *Fireman's Fund Ins. Co. v. Commercial Standard Ins. Co.,* 490 S.W.2d 818, 824 (Tex. 1972);*overruled on other grounds by Ethyl Corp. v. Daniel Constr. Co.,* 725 S.W.2d 705, 708 (Tex. 1987); *Sieber & Calicutt, Inc. v. La Gloria,* 66 S.W.3d 340 (Tex. App.-Tyler 2001, *no writ*) and *Amerada Hess Corp. v. Wood Group Production Technology,* 30 S.W.3d 5 (Tex.App. [14th Dist.] 2000, *writ denied*); *Texas Property Casualty Ins. Gty. Ass'n v. BSA,* 947 S.W.2d 682 (Tex.App.-Austin 1997); *Getty Oil Corp. v. Duncan,* 721 S.W.2d 475, 477 (Tex. App.--Corpus Christi 1986, *writ ref'd n.r.e.*). Absent an unconditional contractual right to settle, an Indemnified Person who settles a claim without obtaining a judicial determination of his liability, assumes in his action for reimbursement, the burden of proving facts that might have rendered him liable to claimant, as well as the reasonableness of the amount he paid. *Aerospatiale Helicopter Corp. v. Universal Heath Services, Inc.,* 778 S.W.2d 492, 500 (Tex. App.--Dallas 1989), *cert. denied*, 498 U.S. 854, 111 S. CT. 149, 112 L.Ed.2d 115 (1990). Determining whether a settlement of a wrongful death case is reasonable involves experience and specialized knowledge. An attorney must review and analyze, among other things, the underlying facts, the identity of the defendant, the damage elements available to a plaintiff, the specific injuries or losses incurred by a plaintiff, the settlement amounts received in similar cases, the complexity of the case, as well as the strength and resources of the opposing counsel. *See Burrow v. Arce,* 997 S.W.2d 229 (Tex. 1999). *Also see Sieber & Calicutt, Inc. v. La Gloria,* 66 S.W.3d 340(Tex.App.-Tyler 2001, *no writ*) where court found that La Gloria settlement was reasonable, prudent and made in good faith and thus was to be reimbursed by Sieber & Calicutt pursuant to the indemnity agreement between La Gloria and Sieber & Calicutt. The court in *Amerada Hess Corp. v. Wood Group Production Technology,* 30 S.W.3d 5 (Tex.App. [14th Dist.] 2000,

writ denied) upheld a settlement as being reasonable and entirely covered by the indemnity agreement even though another defendant was also released because the expert's testimony supported the trial court's finding that the settlement amount was reasonable as to the Indemnified Person's potential liability independent of the other released defendant's potential liability; no apportionment of the settlement amount was required.

(b) Good Faith. An Indemnified Person can not recover to reimburse himself for amounts paid in settlement, if the settlement was not made in good faith. *H.S.M. Acquisitions, Inc. v. West,* 917 S.W.2d 872, 880 (Tex. App.--Corpus Christi 1996, *writ denied*). Additionally, even though an indemnity agreement vests settlement authority in the Indemnified Person, a contractual requirement of settling in "good faith" can lead to liability on the part of the settling Indemnified Person. The court in *H.S.M. Acquisitions, Inc.* found the terms of an agreed judgment between a claimant and the Indemnified Person to be collusive, in part because the settling parties agreed to keep the terms of the judgment confidential and not to file an abstract or other public notice of the judgment.

In *Associated Indemnity Corp. v. CAT Contracting, Inc.,* 918 S.W.2d 580 (Tex. App.--Corpus Christi 1966, *no writ*), the court found that an Indemnified Person breached a covenant of good faith contained in the settlement authorization provision of an indemnity agreement supporting a performance bond when the bonding company (Surety) settled a bond claim without adequate investigation of the circumstances of the claim, and without advance notice to the principal and an opportunity for the principal to argue its case with the obligee. The court further found a common law duty of good faith and fair dealing under these circumstances, the breach of which gave rise to mental anguish damages on the part of the owners of the principal. The provision in the indemnity agreement granted the following settlement authority:

Provision:

> The Surety shall have the exclusive right to decide and determine whether any claim, liability, suit or judgment made or brought against the Surety or the indemnitors or any one of them on any such bond shall or shall not be paid, compromised, resisted, defended, tried or appealed, and the Surety's decision thereon, if made in *good faith*, shall be final and binding upon the indemnitors. An itemized statement of the payments by the Surety for any of the purposes specified herein, sworn to by an officer of the Surety, or the voucher or vouchers for such payments, shall be *prima facie* evidence of the liability of indemnitors to reimburse the Surety for such amounts, with interest. (Emphasis added by author.)

G. Settlement Agreements.

1. Effect of Settlement by Plaintiff with a Joint Tortfeasor.

a. One Recovery Rule: Credit for Settlement Payments. Although the court in *Kenneth H. Hughes Interests v. Westrup* found that the defendant (landlord) was liable to the plaintiff (tenant), the landlord's $23,000 liability was more than offset by the $770,000 settlement payment made by its joint defendants, a contractor (which had indemnified the landlord) and the contractor's subcontractor. The court followed the "one recovery" rule announced in *Stewart Title Guaranty Co. v. Sterling,* 822 S.W.2d 1 (Tex. 1991). In that case, the supreme court held that "(t)here can be but one recovery for one injury, and the fact that more than one defendant may have caused the injury or that there may be more than one theory of liability does not modify this rule. *Sterling,* at 8; and *Ojeda de Toca v. Wise, 748 S.W.2d* 449 (Tex. 1988). *Kenneth H. Hughes Interests v. Westrup*, 879 S.W.2d 229, 233-34, 240 (Tex. App.- Houston [1st Dist.] 1994, *writ denied*).

b. Effect of Settlement (by Release and Indemnity) by Plaintiff of a Joint Tortfeasor Which Also is an Indemnifying Person. In *Martinez v. Gulf States Utility Co.,* 864 S.W.2d 802 (Tex. App.--Houston [14th Dist.] 1993, *writ denied*) the plaintiffs, who were injured when they accidentally touched a high voltage wire, were held to be precluded from recovering against Gulf States, the utility company and owner of the utility pole, because they had previously settled their claim with the contractor, which owed a statutory indemnity to the utility company for such type of accidents. Plaintiff, Daniel Hernandez, was killed, and plaintiffs, Clarence Thompson, Sr. and David Martinez, were injured, in repairing a water well for the defendant property owners, Clarence Thompson, Jr. and Pamela Mendez. Hernandez was killed when Clarence Thompson, Sr., Martinez and Hernandez accidentally touched a high voltage wire.

The court found that a *circuit of indemnity*, created by statute and by contract (the release agreement), had been created by the settlement agreement that precluded recovery by the plaintiff against the utility company. In settling with the property owners, Thompson Jr. and Mendez, the plaintiffs executed a typical release releasing these defendants "for any and all claims, demands ... and causes of action ... whether in contract or in tort ... for and on account of injuries sustained ... (including) any liability for any cross actions seeking contribution and indemnity. ..." TEX. HEALTH & SAFETY CODE ANN. § 752.008 (Vernon 1992) creates a statutory indemnity by persons responsible for having workers near utility lines if they do not follow the advance notice and precautionary procedures established to protect against these type of accidents.

The court found that a *circuit of indemnity* existed precluding recovery against the utility company since the utility company had a statutory indemnity by the settling defendants, who had a contractual indemnity (release) from the plaintiffs.

c. Express Negligence Rule And Settlement Agreements.

(1) The Settlement Agreement Itself. The court in *Martinez v. Gulf States Utility Co*., 864 S.W.2d 802 (Tex. App.--Houston [14th Dist.] 1993, *writ denied*), also held that the express negligence doctrine was not applicable to the release executed as a part of the settlement agreement since the plaintiff could not claim surprise as to the cross claim by the

utility company against the settling defendant for statutory indemnity. The release explicitly contemplated cross actions by the other co-defendant. Liability was certain. *Id.* at 805.

(2) Settlement Authority. If the indemnity clause does not pass the express negligence test and the plaintiff's injuries arise from a negligence claim or through a strict liability claim against the Indemnified Person, then the Indemnifying Person is not liable for a settlement negotiated by the Indemnified Person, even though the indemnity agreement contains an absolute power to settle. *Coastal States Crude Gathering Co. v. Natural Gas Odorizing, Inc.*, 899 S.W.2d 289 (Tex. App.--Houston [15th Dist.] 1995, *no writ*)- -Coastal not able to collect back on $10,500,000 settlement paid to persons injured by fire and explosion fueled by propane gas odorized and sold by Coastal using odorizing chemicals supplied by Natural Gas Odorizing. Indemnity agreement failed to mention liability arising out of strict liability and was contained on back of purchaser order in inconspicuous fashion (same black ink as rest of order form). The court quoted *Fisk Electric Co. v. Constructors & Associates, Inc.,* 888 S.W.2d 813 (Tex. 1994) in rejecting Coastal's argument that the express negligence test was not applicable where absolute settlement authority granted to the Indemnified Person:

> The *Fisk* court made explicitly clear that allowing the rule proposed by Coastal would "leave indemnitors vulnerable to indemnitees who might settle cases without admitting negligence, leaving the indemnitor to pay the costs of settlement and defense." *Id.* at 815. The court further stated in a footnote that even if a settlement could be contested by the indemnitor, such a result would retard, rather than advance, the policy of preventing satellite litigation surrounding interpretation of indemnity clauses.

2. Covenants Not to Execute. In *Ard v. Gemini Exploration Co. and Resolve Drilling Co.,* 894 S.W.2d 11 (Tex. App.-- Houston [14th Dist.] 1994, *writ denied*), the court found that a covenant by an injured employee (Ard) of the Indemnifying Person (RRS Services, Inc.) not to execute (a "covenant not to execute") upon the assets of the Indemnified Person (Resolve) did not extinguish the liability of the Indemnified Person in such a manner as would prevent the Indemnified Person and the injured party from realizing upon the Indemnified Person's excess liability insurance policy. "Therefore, the fact that the indemnitee, Resolve, will not have to pay any damages does not eradicate Resolve's liability, nor does it eradicate an indemnitor's or an insurer's duty to pay." The "covenant not to execute" was the result of insurance settlement paid by the Indemnified Person's primary insurance carrier.

A covenant not to execute is a contract rather than a release. *See Garcia v. Am. Physicians Ins. Exch.,* 812 S.W.2d 25, 33 (Tex. App.--San Antonio 1991), *rev'd on other grounds,* 876 S.W.2d 842 (Tex. 1994); *Y.M.C.A. of Metro. Ft. Worth v. Commercial Standard Ins. Co.,* 552 S.W.2d 497, 595 (Tex. App.--Ft. Worth 1977), *writ ref'd n.r.e., per curiam,* 563 S.W.2d 246 (Tex. 1978). Its legal effect is similar to a "covenant not to sue" because it does not eliminate a damage award; the underlying tort liability remains. *Garcia,* 812 S.W.2d at 32-33; *Y.M.C.A.,* 552 S.W.2d at 505. *Also generally see RTC v. Northpark Joint Venture,* 958 F.2d 1313 (5th Cir. 1992) where the court rejected the argument of a guarantor that it had no liability on its guaranty because the debt guaranteed was a non-recourse liability of the note maker.

3. Insurer's Duty to Insured. The various duties of an insurer to its insured are illustrated by *Crum & Forster, Inc. v. Monsanto Co.,* 887 S.W.2d 103 (Tex. App.--Texarkana 1994, *no writ*) where Monsanto was awarded $71,048,070.22 for actual and treble damages, prejudgment interest and attorney's fees arising out of the insurer's obtaining a financial interest in, and control of, litigation against its insured in an attempt to defeat the insured's reimbursement rights under an environmental impairment liability policy. INS. CODE Art. 21.21 § 16(a) (Vernon 1981) violation.

H. Framework for an Indemnity Provision.

1. Provision Protecting Indemnified Person From Sole or Concurring Negligence. *See* the indemnity provisions contained in the Appendix of Forms. *Also see* the clauses proposed by Richard L. Scheer in Scheer, *Model Contractual Indemnity Provisions Effective to Protect an Indemnitee Against His Own Negligence or Other Fault*, 50 TEX. B.J. 602 (Jun. 1987) and Ellis and Kessler, *Exculpation and Indemnity Clauses*, 23RD ANNUAL MORTGAGE LENDING INSTITUTE (UNIV. TEX. 1989); Civins, *Dealing with Environmental Issues in Real Estate Contracts*, 3RD ANNUAL ADVANCED REAL ESTATE DRAFTING COURSE C (STATE BAR OF TEXAS PDP 1992); Schwenke, *Hazardous Waste: Hazardous Headache to Borrowers and Lenders*, 22ND ANNUAL MORTGAGE LENDING INSTITUTE (UNIV. TEX. 1988) for extensive Appendix of environmental indemnity agreements and related agreements; and Rider and Shuly, *Environmental Considerations in Negotiating and Drafting Commercial Real Estate Documents*, 1ST ANNUAL ADVANCED REAL ESTATE DRAFTING COURSE I (STATE BAR OF TEXAS PDP 1990). Pierce, *Structuring Routine Oil and Gas Transactions to Minimize Environmental Liability,* 33 WASHBURN L. J. 76 (1993); Parker and Slavich, *Contractual Efforts to Allocate the Risk of Environmental Liability: Is There a Way to Make Indemnities Worth More Than the* Paper They are Written On?*,* 44 SW. L. J. 1349 (1991); Hass and Roska, *Environmental Indemnities and Other Environmental Provisions in the Purchase and sale of Mineral Properties*, 38 ROCKY MTN. MIN L. INST. 22-1 (1992).

The following "model" indemnity agreement has the following **components**:

(1) Prerequisites to its validity. A choice of laws provision; drafted to comply with common law (the fair notice requirements) and statutory requirements (to address the Workers' comp bar; recognition of the limits of coverage for certain architect's liabilities).

(2) Events triggering the indemnity obligation. Listing of the "**Indemnified Matters**" as to which Indemnified Liabilities are indemnified.

(3) The scope of the Indemnified Liabilities. Definition of the "**Indemnified Liabilities**", including the types of Liabilities Covered (sole, concurrent, strict, statutory, employee injuries, disease, gross), the types of Liabilities listed as Excluded Matters, time period covered, types of damages covered (actual, consequential, fines, punitive).

(4) The settlement and defense procedures. The procedures for responding to claims covered by the indemnity (managing the defense and settlement of the claim, selection of counsel, time limit for giving notice of claim, the handling of the pursuit of other remedies such as available insurance).

(5) The parties to the indemnity. Definition of the "**Indemnifying Persons**" and the "**Indemnified Persons**" (parent, subsidiaries, officers, directors, successors, assigns, beneficiaries).

(6) The remedies for enforcement of the indemnity. Supporting insurance, releases, waivers, attorneys' fees for enforcing indemnity.

The following "**pitfalls**" may be associated with indemnity provisions:

(1) Unlimited Liability. Contractual indemnities are commonly unlimited as to the dollar liability covered, unlike insurance which is written for specified limits; does not have deductibles; and may not be limited to available insurance.

(2) Broad Risks Covered. Contractual indemnities are commonly broader in scope than the insurance program provided in the same contract. For example, commercial general liability insurance covers "bodily injury" whereas contractual indemnities may be worded with language different than or broader than the coverage terms of the CGL policy, such as indemnifying as to "injuries" or "personal injuries".

(3) Financial Strength of Indemnifying Person. Contractual indemnities are dependent upon the financial strength of the Indemnifying Person.

Attached as Appendix 3 is a comparison of the indemnity provisions contained in the 1977 Edition and the 1997 Edition of the AIA A201 General Conditions of the Construction Contract. Note that none of the provisions are differentiated from other provisions in the AIA forms and therefore are not more conspicuous than other provisions and do not expressly refer either to the negligence or strict liability of the Indemnified Person as being covered.

Provision: 1997 Edition A201 General Conditions of the Construction Contract

3.18.1 To the fullest extent permitted by law, the Contractor shall indemnify and hold harmless the Owner, the Architect, the 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, provided that such claim, damage, loss or expense is attributable to *bodily injury, sickness, disease or death, or to injury to or destruction of tangible property (other than the Work itself) including loss of use resulting therefrom*, but only to the extent caused in whole or in part by negligent acts or omissions of the Contractor, a Subcontractor, anyone directly or indirectly employed by them or anyone for whose acts they may be liable, regardless of whether or not such claim, damage, loss or expense is caused in part by a party indemnified hereunder. Such obligation shall not be construed to negate, abridge, or reduce other rights or obligations of indemnity which would otherwise exist as to a party or person described in this Paragraph 3.18. (Underlining and *italics* added by author).

The underlined reference to "regardless ... caused in part by a party indemnified hereunder" neither covers expressly the concurrent negligence of the Owner nor liability incurred by the Owner arising out of strict liability. The same deficient language is used in the AIA A401 Standard Form of Agreement Between Contractor and Subcontractor.

The Indemnified Liabilities covered by the AIA language "bodily injury, sickness, disease, or death, or to injury or to destruction of tangible property (other than the Work itself), including loss of use there from" tracks the coverage language of the CGL policy, thereby limiting the liabilities covered to the matters covered by the insurance, except there is no deductible and no upside limit.

2. Provision for Contractual Comparative Responsibility. A system of contractual comparative responsibility might be introduced. The following is an example of an indemnity provision for a Lease employing contractual comparative responsibility (*also see* **Appendix 7**):

Provision:

1. ***Tenant's Indemnity***. _____.

2. ***Landlord's Indemnity***. _____.

3. ***Concurrent Negligence, Products Liability and/or Breach of Warranty*. If a claim or cause of action arises out of the joint or concurrent causation, responsibility or fault, whether negligence, strict liability in tort, gross negligence, breach of warranty, express or implied, products liability, breach of the terms of this Lease or willful misconduct of the parties hereto or their Instrumentalities, each of Landlord and Tenant shall indemnify the other to the extent that the indemnifying party's or its Instrumentality's negligence, strict liability in tort, gross negligence, breach of warranty, express or implied, products liability, breach of the terms of this Lease or willful misconduct causes or contributes to the loss, claim, judgment or liabilities.**

4. ***Settlement*. It is expressly agreed that in the event either party should fail or refuse to participate in settlement of a**

claim for damages the other party may settle with the claimant without prejudice to such party's indemnity rights set forth herein, it being expressly recognized that a settlement, after demand shall be made on the non-settling party hereto, constitutes a settlement of the proportionate fault, including but not limited to, negligence of both parties hereto, which proportionate fault may later be apportioned between the parties hereto. Another comparative negligence approach not involving cross indemnities is to limit indemnity to the percentage of negligence of the Indemnifying Person.

Provision:

Notwithstanding the foregoing, Tenant's obligation to indemnify the Indemnified Persons shall extend only to the percentage of responsibility of Tenant and of Tenant's Instrumentalities in contributing to such Liabilities.

A further approach is to limit liability to cases where the Indemnified Person's percentage of liability exceeds the Indemnifying Person's percentage of liability.

Provision:

Notwithstanding the foregoing, Tenant's obligation to indemnify the Indemnified Persons shall apply only where the percentage of negligence of Tenant and of its Instrumentalities in contributing to the Liability exceeds the negligence of the Landlord and its Instrumentalities.

Also see Sieber & Calicutt, Inc. v. La Gloria, 66 S.W.3d 340 (Tex.App.-Tyler 2001, *no writ*) where the court found that Sieber & Calicutt was at least equally negligent as was La Gloria and therefore La Gloria was entitled to recover indemnity of one-half of the amount it paid in settlement of a wrongful death suit brought on behalf of one of its deceased employees. The indemnity provision limited Sieber & Calicutt's indemnity to it proportionate share of liability if its liability was equal to or less than La Gloria's liability. The La Gloria indemnity provision reads as follows:

Provision:

Contractor (Sieber & Calicutt) agrees to hold harmless and unconditionally indemnify La Gloria, its directors, officers, agents, representatives and employees against and for all liability, costs and expenses, claims and damages which La Gloria at any time suffer or sustain or become liable for by reason of any accidents, damages or injuries either to the persons or property or both, of Contractor, its subcontractors and suppliers, or to the persons or property of La Gloria, its subcontractors and suppliers, arising in any manner from the Work performed hereunder, including but not limited to any negligent act or omission of La Gloria, its directors, officers, agents, representatives or employees, provided however, that if the negligence of La Gloria shall be found to be greater than or equal to the comparative negligence of the Contractor, then the Contractor shall only be liable to La Gloria to the extent of the Contractor's own negligence.

I. Environmental Indemnities.

1. CERCLA. CERCLA contains a specific provision recognizing the validity of indemnity agreements. Section 9607(e) provides:

(1) No indemnification ... agreement ... shall be effective to transfer from the owner or operator of any ... facility or from any person who may be liable for a release or threat of release under this section, to any other person the liability imposed under this section. Nothing in this Subsection shall bar any agreement to insure, hold harmless, or indemnify a party to such agreement for any liability under this section.

(2) Nothing in this subchapter, including the provisions of paragraph (1) of this Subsection, shall bar a cause of action that an owner or operator or any other person subject to liability under this Section or a guarantor, has or would have, by reason of subrogation or otherwise against any person.

CERCLA, 42 U.S.C.A. § 9607(e) (1983).

Although a responsible party can not "shift" its statutory "liability," it can obtain an indemnity (agreement to be reimbursed) for such liability, thereby shifting the financial loss arising out of such liability. *Joslyn Manufacturing Co. v. Koppers Co., Inc.,* 40 F.3d 750 (5th Cir. 1994)--even if the indemnity agreement does not specifically mention CERCLA or even "environmental contamination." This case involved the assumption by the assignee of the lessee's liabilities under a lease. The lease contained a broad form indemnity agreement. The lease predated CERCLA and provided for indemnification for "all" liabilities arising out of the condition of or defect in the premises. The court found that the indemnity included CERCLA response costs for contamination by the assignor/lessee which predated the assignment to the assignee. *See* Welborn, *Environmental Liabilities of Landlords in Commercial Leasing: Avoidance and Indemnities from the Landlord's Perspective*, ALI-ABA Modern Real Estate Transactions (1996), Committee on Environmental Controls, *Environmental Indemnification--A Practical Approach to Risk Allocation*, ABA Section of Business Law 1993 Annual Meeting (N.Y.); M. Ellis, *Private Indemnity Agreements Under Section 107 of CERCLA,* 22 ENV'T REP. (BNA) 1953 (Dec. 6, 1991); Haas and Roska, *Environmental Indemnities and Other Environmental Provisions in the Purchase and Sale of Mineral Properties*, 38 ROCKY MTN. MIN. L. INST. 22-1, 22-37 to 22-43 (1992); and Parker and Slavich, *Contractual Efforts to Allocate the Risk of Environmental Liability: Is There a Way to Make Indemnities Worth More Than the Paper They are Written On?,* 44 SW. L.J. 1349, 1363-64 (1991).

The allocation of environmental risks in a sales transaction through representations, warranties, and

indemnities will generally result in a contractual assumption of liability.

In cases where a condition is known to exist, a preferable method may be to provide for an express assumption of liability. An environmental indemnity agreement may be employed to shift back to the seller a potential cleanup risk arising out of detected marginal contaminations that are below reportable levels, but significant enough to trigger agency action if the condition comes to the attention of the governmental agency.

2. Interpretation under Applicable Law. There is a disagreement among courts as to whether a "uniform" federal common law or state law should be applied in interpreting indemnity agreements under CERCLA. *Compare Mardan Corp. v. C.G.C. Music, Ltd.,* 804 F.2d 1454, 1458 (9th Cir. 1986)--applying state law with *Wiegmann & Rose Int'l Corp. v. NL Industries,* 735 F. Supp. 957, 962 (N.D. Cal. 1990)--adopting a uniform federal rule.

3. Oilfield Anti-Indemnity Statute. The Texas Oilfield Anti-Indemnity Statute which prohibits indemnity agreements in oil and gas service contracts that seek to encompass the Indemnified Person's own negligence or fault, does not apply to a surface estate owner who imposes indemnity obligations on its lessee and other developers. Section 127.04(2) TEX. CIV. PRAC. & REM. CODE ANN. (Vernon 1997) provides:

> This Chapter does not apply to loss or liability for damages or an expense arising from:
>
> (2) property injury that results from pollution, including cleanup and control of the pollutant....

See discussion of the Texas Oilfield Anti-Indemnity Statute at **Article IID4c–Contractual Indemnity - Elements - Statutory Limits on Indemnity - Oil and Gas Service Contracts** above.

III. Coordination with Insurance Coverage.

A. Types of Insurance. Lawless, *Insurance Coverage for Construction Liabilities*, 9TH ANNUAL CONSTRUCTION LAW CONFERENCE (STATE BAR OF TEXAS 1996); Hosford, *Keeping Covered--Drafting Insurance Clauses in Leases, Loan Documents and Construction Contracts,* 7TH ANNUAL ADVANCED REAL ESTATE DRAFTING COURSE N (STATE BAR OF TEXAS 1996); LeBarron, *Drafting Insurance Provisions*, 4TH ANNUAL ADVANCED REAL ESTATE DRAFTING COURSE (STATE BAR OF TEXAS 1993); Walts, Ed, *General Liability Insurance Provisions and Indemnities and Property and Casualty Insurance Policies*, ADVANCE REAL ESTATE LAW SEMINAR N (STATE BAR OF TEXAS 1993).

1. Liability Insurance.

a. Workers' Compensation and Employers' Liability Insurance. Although an Indemnifying Person's (tenant's, contractor's or subcontractor's) workers' compensation insurance will not eliminate the potential liability of the Indemnified Person (the landlord, owner or contractor in the above parenthetical examples), it may provide a buffer against potential claims and make it less likely that the Indemnified Person will be sued by an injured employee of the Indemnifying Person. Because workers' compensation statutes limit the recovery by an injured employee from the employer, an indemnification provision is appropriate so as to ensure that the employer remains ultimately liable for damages in excess of the statutory workers' compensation limits.

(1) Waiver of Subrogation. As noted below, in order to avoid the workers' compensation carrier suing the Indemnified Person to obtain contribution and reimbursement for amounts paid by the carrier to the employee, the parties should obtain a waiver of subrogation endorsement in favor of the Indemnified Persons. The right of a workers compensation insurer to subrogate against a third party who may have caused an employee injury is recognized by statute. TEX. LABOR CODE § 417.001 (Vernon 1996) provides as follows:

> **417.001. Third Party Liability.**
>
> (a) An employee or legal beneficiary may seek damages from a third party who is or becomes liable to pay damages for an injury or death that is compensable under this subtitle and may also pursue a claim for workers' compensation benefits under this subtitle.
>
> (b) If a benefit is claimed by an injured employee or a legal beneficiary of the employee, the insurance carrier is **subrogated** to the rights of the injured employee and may enforce the liability of the third party in the name of the injured employee or the legal beneficiary. If the recovery is for an amount greater than that paid or assumed by the insurance carrier to the employee or the legal beneficiary, the insurance carrier shall:
>
> (1) Reimburse itself and pay the costs from the amount recovered; and
>
> (2) Pay the remainder of the amount recovered to the injured employee or the legal beneficiary.

Since a workers compensation insurer pays benefits on a strict liability basis, it is entitled to receive the first dollars of any recovery by the employee from a third party to the extent that party caused or contributed to the injury rather than the employer.

In most states, workers compensation insurance is written on the 1992 edition of the Workers Compensation and Employers Liability Insurance Policy form (WC 00 00 01 A) developed by the National Council on Compensation Insurance (***"NCCI"***). This form is *silent* with respect to a pre-loss waiver by employer. Therefore, a waiver of subrogation executed prior to a loss should prevent the insurer from subrogating against the third party, even without an endorsement to the policy. The NCCI has drafted an advisory endorsement for use with the standard policy (WC 00 03 13). This endorsement reads as follows:

> We have the right to recover our payments from anyone liable for an injury covered by this policy. We will not enforce our right against the person or organization named in the Schedule. (This agreement applies only to the extent that you perform work under a written contract that requires you to obtain this agreement from us.)
>
> This agreement shall not operate directly or indirectly to benefit anyone not named in the Schedule.

A premium as high as 2% of the total policy premium might be charged for the endorsement, if requested on a blanket basis (usually between $500- $1,500). When requested on a specific project, the charge is usually 2 to 5% of the premium attributable to the project to which it applies, if it can be so segregated.

(2) Workers' Compensation Bar. A contractual indemnity by the employer of the Indemnified Person is necessary to overcome the Workers' Compensation Bar so as at least to pass back to the employer the employer's percentage of responsibility (if not all of the employee's damages in excess of the statutory workers' compensation limits to the employer's liability) which might otherwise be borne by the Indemnified Person absent the indemnity. The contractual indemnity should also be drafted to pass back to the employer the costs of defense of the employee's claim.

(3) Employer's Liability Coverage. It is important for the Indemnified Person to require the Indemnifying Person to obtain Employer's Liability Insurance in order to afford employer insurance coverage for risks not covered by workers' compensation insurance (*e.g.*, gross negligence of the employer) and persons not covered by workers' compensation insurance (*e.g.*, indirect damages as a result of the worker's injuries, due to spouses and dependents, loss of consortium and loss of income).

b. Commercial General Liability Insurance. Commercial General Liability (***"CGL"***)

Insurance provides broad liability coverage. It is similar to an "all risk" policy in that it provides coverage against liabilities unless specifically excluded. CGL policies usually include the cost to defend the insured in addition to the insured loss. A CGL policy has the following three basic coverages:

(1) Bodily Injury and Property Damage. This coverage is for amounts which the insured is legally obligated to pay as damages as a result of bodily injury or property damage occurring (if the policy is an "occurrence" policy), or arising out of claims made (if it is a "claims made" policy), during the policy period, and such bodily injury or property damages are caused by an accident occurring within the coverage territory specified in the insurance policy. The "commercial" general liability policy form has been in use since **1986**. It is broader in scope than the "comprehensive" general liability policy form. Both forms are in use nationally. A commercial general liability policy automatically includes coverage extensions for Contractual Liability, Personal Injury Liability, Host Liquor Liability, Broad Form Property Damage Liability and eight other extensions, which previously had to be included by endorsement.

Most commercial general liability policies include the following six separate "limits" of liability:

(1) Each Occurrence.
(2) General Aggregate.
(3) Product and Completed Operations.
(4) Personal Injury Liability.
(5) Fire Damage Liability.
(6) Medical Expense.

The Occurrence limit is the maximum payable for claims arising out of any one occurrence.

The General Aggregate limit is the maximum payable for all claims during the year arising out of occurrences other than Product and Completed Operations losses. The General Aggregate limit can be broadened by two different endorsements:

(1) **Aggregate Limit Per Location Endorsement**. This endorsement applies the General Aggregate limit separately to each "location" owned by or rented to the insured.

(2) **Aggregate Limit Per Project Endorsement**. This endorsement is used for construction contracting and similar risks. This endorsement applies the General Aggregate limit separately to each project away from the premises owned by or rented to the insured, without limitation on the number of projects.

The Product Aggregate limit is the maximum payable for all claims during the year arising out of product and completed operations exposures. Product and Completed Operations coverage still must be endorsed onto CGL policies and is not automatically covered.

The triggering term for coverage was changed in **1966** from "**accident**" to "**occurrence**". "**Occurrence**" is now defined in CGL policies as:

> an accident, including continuous or repeated exposure to conditions, which results, during the policy period, in bodily injury or property damage neither expected nor intended by the insured.

The "occurrence" definition broadened the scope of coverage afforded by its "accident"-based predecessor in two important ways. First, it specifically recognized coverage for injuries resulting from long-term exposure to conditions (as distinguished from an abrupt event). Second, it clarified that the policy covered the unintended consequences of intentional acts.

Texas courts have struggled with the concept of an intentional act resulting in unintended injury.

In the 1967 case, *Massachusetts Bonding and Ins. Co. v. Orkin Exterminating Co.,* 416 S.W.2d 396, 400 (Tex. 1967), involving a coverage dispute under a pre-1966 "accident"-based CGL policy for property damage resulting from the negligent application of the pesticide Lindane, the Texas Supreme Court held that the term "accident" as used in the policy included "negligent acts of the insured causing damage which is undesigned and unexpected". The court of appeals had stated in coming to the same conclusion that "(s)ince the claim ... was predicated on acts committed negligently, even in violation of the law, but not with the intent to inflict injury, such claim was within the coverage of the insurance policy". *Orkin Exterminating Co. v. Massachusetts Bonding and Ins. Co.,* 400 S.W.2d 20, 27 (Tex. Civ. App.--Houston 1965), *rev'd on other grounds,* 416 S.W.2d 396 (Tex. 1967).

In *Argonaut Southwest Ins. Co. v. Maupin,* 500 S.W.2d 633 (Tex. 1973), the Texas Supreme Court appears to have limited *Orkin* to those situations where the acts resulting in damage are "negligent", as opposed to "willful or intentional". In *Maupin*, a state highway contractor entered into an agreement to purchase borrow material from Kipper. The contractor entered onto the property believed to be owned by Kipper and removed 5,774 cubic yards of borrow material. It was later determined that Kipper did not own the property, and thus, the real landowners sued the contractor in *trespass*. The contractor filed a claim under his "occurrence"-based liability policy contending that the removal of the material was an occurrence or accident. In rejecting coverage under the policy, the Texas Supreme Court held:

> where the **acts** [removing the material] are voluntary and intentional and the injury is the natural result of the act, the result was not caused by accident even though the result may have been unexpected, unforseen and unintended.

Maupin, 500 S.W.2d at 635. One commentator argues that the supreme court failed to understand the intent of the insurance industry policy drafters that the term "occurrence" encompasses the unintended consequences of intentional acts and that the court's decision may have been swayed by the fact that the claim--intentional trespass--by definition constitutes an intentional act to injure property. Therefore, the court may have presumed a constructive intent to cause injury. This has resulted in many subsequent courts focusing erroneously on the damage-causing act, as opposed to the resulting harm. Lawless, *Insurance*

Coverage for Construction Liabilities, 9th ANNUAL CONSTRUCTION LAW CONFERENCE 3 (State Bar of Texas 1996).

However, in 1993, in *State Farm Fire & Cas. Co. v. S.S.,* 858 S.W.2d 374 (Tex. 1993), the Texas Supreme Court recognized a distinction between intentional acts and intended injury. The court was called upon the interpret the "intentional injury exclusion" in a homeowners policy in a claim resulting from the transmission of herpes. The court held that coverage was not precluded when the policyholder did not know that his intentional conduct (engaging in sexual intercourse) was "substantially certain" to result in the transmission of the disease. The court found a difference between performing acts that one thinks might cause injury (which are covered), and acts that one knows are "substantially certain" to cause injury (which are not covered). *State Farm Fire & Cas. Co. v. S.S.,* 858 S.W.2d at 378. It is unclear how the supreme court will interpret a coverage issue for bodily injuries which are unintended but the result of an intended act.

(2) Personal or Advertising Injury. "Personal injury" is defined in the CGL policy as injury (other than bodily injury) arising out of false arrest, malicious prosecution, wrongful entry or eviction, or written slander or libel, or certain violations of privacy.

(3) Medical Payments. Medical Payments Coverage covers medical payments arising out of the bodily injury caused by an accident to certain persons other than the insured.

(4) Exclusions. By its very nature as third-party liability insurance, CGL policies exclude coverage for losses to an insured's own personal or real property. The primary reason for the exclusions in the CGL policies is that separate lines of coverage are available in the market place for these specific risks (*e.g.,* property insurance, workers' compensation insurance, automobile insurance). Some of the exclusions to coverage are for the following:

(a) Intentional Acts. Bodily injury or property damage expected or intended by the insured, excepting the use of reasonable force to protect property or persons.

(b) Alcohol. Bodily injury or property damage related to certain uses of or occurrences associated with alcohol. (This exclusion may necessitate requiring the Indemnifying Person to obtain a Liquor Liability Policy.)

(c) Workers' Compensation and Employers' Liability Insurance Coverage.

(d) Pollution. Certain damages resulting from pollution or release of hazardous materials.

The so-called "pollution exclusion" to coverage has been the subject of much controversy and recent litigation. *See* Lawless, *Insurance Coverage for Construction Liabilities,* 9th ANNUAL CONSTRUCTION LAW CONFERENCE 11-32 (State Bar of Texas 1996) for an extensive review of cases and regulatory history concerning the "pollution exclusion" in CGL policies.

The 1966 CGL policy was generally interpreted to cover bodily injuries and property damage caused by gradual pollution events as long as the resulting injuries or damages were neither "expected nor intended" by the insured, notwithstanding that the release or discharge of the pollutants may have been intentional.

In 1970 insurers developed a standardized pollution exclusion, which was adopted by the Texas State Board of Insurance in 1970 as a mandatory endorsement to all CGL policies effective in Texas on or after July 8, 1970. Order No. 13844, Texas State Board of Insurance, approving Manuals of Liability Insurance-Contamination or Pollution Exclusion and Endorsements (May 29, 1970). The 1970 CGL pollution exclusion endorsement reads as follows:

Provision: 1970 Pollution Exclusion Endorsement

> It is agreed that the insurance does not apply to bodily injury or property damage arising out of the discharge, dispersal, release or escape of smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, liquids or gases, waste materials or other irritants, contaminants or pollutants into or upon land, the atmosphere, or any water course or body of water; but this exclusion **does not apply** if such discharge, dispersal, release or escape is **sudden** and **accidental**.

The Insurance Rating Board ("***IRB***") and the Mutual Insurance Rating Board ("***MIRB***"), now known as the Insurance Services Office, Inc. ("***ISO***"), and the sponsors of the change to the CGL policies, provided the State Board of Insurance with the following official "explanation" concerning the scope and effect of the pollution exclusion endorsement:

> Coverage for pollution or contamination is not provided in most cases under present policies because the damages can be said to be expected or intended and thus are excluded by the definition of occurrence. The [standard-form pollution] exclusion clarifies this situation so as to avoid any question of intent. Coverage is continued for pollution or contamination caused injuries when the pollution or contamination results from an accident....

It is instructive to take note of the following criticisms of this "explanation" contained in *Morton International, Inc. v. General Acc. Ins. Co.,* 134 N.J. 1, 629 A.2d 831, 852 (N.J. 1993), *cert. den'd sub nom.; Ins. Co. of N. America v. Morton International Co., 114 S.Ct. 2764, 129 L.Ed.2d 878 (1994)* as commented upon in Lawless, *Insurance Coverage for Construction Liabilities,* 9th ANNUAL CONSTRUCTION LAW CONFERENCE 19-20 (State Bar of Texas 1996). In examining the IRB's explanation of the 1970 pollution exclusion, the New Jersey Supreme Court in *Morton* concluded that "[t]he first sentence of the IRB's explanation is simply not true." The insurance industry had drafted the 1966 "**occurrence**" based general liability policy to cover property damage for gradual pollution, with no restriction on the "suddenness" of the pollution discharge. Indeed, the "occurrence"-based

policy "seemed tailor made to extend coverage to most pollution situations." Rosenkranz, Note, *The Pollution Exclusion Through the Looking Glass,* 74 GEO. L. J. 1237, 1251 (1986). The New Jersey court further observed that "The second sentence of the IRB's explanation is even more misleading than the first one. Despite the IRB's assertion that the exclusion merely 'clarifies this situation', the exclusion actually purports to preclude coverage for all coverage for unintentional pollution damage except for that caused by sudden and accidental discharges". *Morton,* 629 A.2d at 852. The New Jersey Supreme Court stated that "[t]o described a reduction of coverage of that magnitude as a 'clarification' not only is misleading, but comes perilously close to deception". *Id.* at 853. That "coverage is continued for pollution or contamination caused injuries when the pollution or contamination results from an accident" contradicts the very wording of the exclusion that coverage is not afforded unless the discharge of pollutants is "**sudden and accidental**". The explanation ignores the "injuries" versus "discharge" distinction and "the conclusion is virtually inescapable that the memorandum's lack of clarity was deliberate." *Morton,* 629 A.2d at 853.

Scope of 1970 Pollution Exclusion. The following cases are instructive on the scope of the 1970 pollution exclusion. *Meridian Oil Production, Inc. v. Hartford Acc. & Ind. Co.,* 27 F.3d 150 (5th Cir. [Tex.]), *reh'g en banc den'd,* 35 F.3d 564 (1994)--pollution damages arising from Meridian's oil and gas activities did not constitute covered occurrences when Meridian's "conduct inevitably and **predictably** caused the pollution"; *In re Texas Eastern Transmission Corp. PCB Contamination Insurance Coverage Litigation,* 870 F.Supp. 1293 (E.D. Pa. 1992)--applying Texas law in holding that the term "**damages**" is ambiguous and that a policyholder's costs of complying with either a demand or an injunction to remediate property damage or bodily injury is recoverable "**as damages**", if incurred primarily because of actual and imminent third-party property damage, bodily injury, or both; *Snyder General Corp. v. Century Indemnity Co.,* 907 F.Supp. 991 (N.D. Tex. 1995), *appeal pending* (5th Cir.)--holding that environmental response costs are not covered damages; *Mustang Tractor & Equipment Co. v. Liberty Mutual Ins. Co.,* 76 F.3d 89 (5th Cir. 1996), *appeal pending* (5th Cir.)–damages do not include contribution and indemnity claims for environmental cleanup costs; also held that "**sudden and accidental**" unambiguously has a temporal component that can mean either (1) an instantaneous or abrupt event or (2) an unexpected incident of limited duration (case involved a solvent leak that occurred within a 24- hour period that was unexpected and therefore a fact issue existed preventing summary judgment against the insured); *American States Ins. Co. v. Hanson Industries,* 873 F.Supp. 17 (S.D. Tex. 1995)-the "sudden and accidental" language in the pollution exclusion is clear and unambiguous, and that the "initial discharge, not the resulting damage, must be [both] sudden and accidental in order to avoid the" exclusion and that the "term '**sudden**' has a temporal meaning of '*quick or abrupt*', not '*unexpected*' or '*unintended*'" (case involved intentional dumping of hazardous wastes at a dump site without knowledge of the substances pollutant content); and *Union Pacific Resource Co. v. California Union Ins. Co.,* 894 S.W.2d 401 (Tex. App.--Ft. Worth 1994, *writ den'd*)--reversed trial court's holding that waste disposal at a landfill over a 3 year period of time was not "**accidental**" as being not the relevant "discharge", but that the "polluting 'occurrence' is the 'discharge, dispersal, release, or escape' or 'seepage, pollution or contamination' of toxic material into the environment".

In 1985 the Texas State Board of Insurance approved the use of a non- mandatory endorsement, which has become to be known as the "**absolute**" pollution exclusion. Order No. 46331, Texas State Board of Insurance, approving an Optional Pollution Exclusion Endorsement (Feb. 19, 1985). The 1985 CGL "absolute" pollution exclusion reads as follows:

Provision: 1985 "Absolute" Pollution Exclusion "(f)"

(f) This insurance does not apply to:

(1) to "bodily injury" or "property damage" arising out of the actual, alleged or threatened discharge, dispersal, release or escape of pollutants:

(a) at or from premises owned, rented or occupied by the named insured;

(b) at or from any site or location used by or for the named insured or others for the handling, storage, disposal, processing or treatment of waste;

(c) which are at any time transported, handled, stored, treated, disposed of, or processed as waste by or for the named insured or any person or organization for whom the named insured may be legally responsible; or

(d) at or from any site or location on which the named insured or any contractors or subcontractors working directly or indirectly on behalf of the named insured are performing operations;

(i) if the pollutants are brought on or to the site or location in connection with such operations; or

(ii) if the operations are to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize the pollutants.

(2) to any loss, cost or expense arising out of any governmental direction or request that the named insured test for, monitor, clean up, remove, contain, treat, detoxify or neutralize pollutants.

Pollutants means any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.

Subparagraphs (a) and (d) (i) of paragraph (1) of this exclusion do not apply to "bodily injury" or "property damage" caused by heat, smoke or fumes from a hostile fire. As used in this exclusion, a hostile fire means one which becomes uncontrollable or breaks out from where it was

intended to be.

The following explanation of the scope and intent of this exclusion is contained in the following statement contained in ISO's filing with State Board of Insurance:

> This endorsement introduces a total pollution exclusion for bodily injury and property damage arising from the discharge of pollutants. The exclusion **does not apply** to damages arising out of **products or completed operations** nor to certain **off- premises discharges** of pollutants.

Scope of 1985 Pollution Exclusion. The following cases are instructive on the 1985 "absolute" pollution exclusion: *National Union Fire Ins. Co. v. CBI Industries, Inc.,* 907 S.W.2d 517 (Tex. 1995)--in this case the Texas Supreme Court held that the "absolute" pollution exclusion unambiguously precluded coverage to the insured for damages and injuries resulting from hydrofluoric acid being released into the atmosphere when a crane's load fell on a pipe connected to a storage tank containing hydrofluoric acid resulting in 60 lawsuits; and the following cases following the lead of the supreme court: *Pro-Tech Coatings, Inc. v. National Standard Ins. Co*., 897 S.W.2d 885 (Tex. App.--Dallas 1995, *no writ*)--Dallas Court of Appeals held that despite the "absolute" pollution exclusion the insurer had a duty to defend Pro-Tech in two suits alleging bodily injuries resulting from exposure in the workplace to products containing asbestos and silica, as well as to other toxic dust, fumes, and vapors, since the court held that Pro-Tech was not performing "operations" at the sites where the exposures took place (the products causing the fumes were manufactured by Pro-Tech and ended up at the sites where the plaintiffs were exposed); *Round Rock Plaza Venture v. Maryland Cas. Co.,* 1996 WL 63956 (Tex. App.–Austin 1996)--held exclusion was ambiguous under the facts of case, in that it was not clear that sewage overflowing from a toilet fell under the definition of "pollutants" or "wastes" in the exclusion; *Constitution State Ins. Co. v. Iso-Tex. Inc.,* 61 F.3d 405 (5th Cir. 1995)–insured causing injuries by exposing third parties to radioactive medical waste excluded from coverage as a "**waste**"; *Navajo Refining Co. v. CIGNA Ins. Co.,* 1995 WL 861201 (S.D. Tex. 1995)--no coverage for release of gasoline from a ruptured pipeline; and *Northborok Ind. Ins. Co. v. Water District Management Co., Inc.*, 892 F.Supp. 170 (S.D. Tex. 1995)--did not cover injuries to public resulting from drinking water from water wells contaminated with benzene.

Owned-or Leased-Property Exclusion

The "owned- or leased-property" exclusion to the CGL policy has been held to preclude coverage for the costs of cleaning up the insured's own property where the contamination is located solely on the insured's property and does not pose a threat to third-party property. *See, e.g., Western World Ins. Co. v. Dana,* 765 F.Supp. 1011 (E.D. Cal. 1991); *United States v. Conservation Chemical Co.,* 653 F.Supp. 152 (W.D. Mo. 1986). Some courts have held that this exclusion does not apply to preclude coverage of cleanup costs on the insured's property when the cleanup is necessary to prevent the migration of pollutants into groundwater or onto adjacent third-party property. *See Gerrish Corp. v. Universal Underwriters Ins. Co.,* 754 F.Supp. 358 (D.Vt. 1990), *aff'd,* 947 F.2d 1023 (2nd Cir. 1991), *cert. den'd,* 112 S.Ct. 2939 (1992); *Bankers Trust Co. v. Hartford Acc. & Ind. Co.* 518 F.Supp. 371 (S.D.N.Y. 1981), *vacated on other grounds,* 621 F.Supp. 685 (S.D.N.Y. 1981); *City of Edgerton v. General Cas. Co*., 493 N.W.2d 768 (Wis. App. 1992), *aff'd in part, rev'd in part on other grounds,* 517 N.W.2d 463 (1994).

A Texas federal district court in *American States Ins. Co. v. Hanson Industries*, 873 F.Supp. 17 (S.D. Tex. 1995) held that under Texas law the surface property owner "owned" the groundwater, and that since the contamination of the groundwater was limited to the insured's property, the "owned-property" exclusion barred recovery. In *In re Texas Eastern Transmission Corp. PCB Contamination Insurance Coverage Litigation,* 870 F.Supp. 1293, 1344 (E.D. Pa. 1992), *aff'd on other grounds,* 15 F.3d 1249 (3rd Cir.), *cert. den'd sub nom. Texas Eastern Transmission Corp. v. Fidelity & Cas. Ins. Co. of N.Y.,* 115 S.Ct. 291, 130 L. Ed.2d 206 (1994), a Pennsylvania federal district court applying Texas law held that the owned-property exclusion did not preclude coverage for costs of cleaning up an insured's property that were "significantly related" to actual third-party harm or to the prevention of future "imminent and substantial" third-party damages Recently, a Wisconsin court of appeals court held that a CGL policy's pollution exclusion did not apply to the property damage provisions of the product and completed operations coverage. The court determined that the products and completed operations coverage contained its own exclusions--but not the pollution exclusion. Additionally, the court decided that the owned and operated property exclusion did not apply, finding that contaminated ground water was not "property owned or operated" by the gas station owner, but was owned by the people of Wisconsin. Therefore, although the owned property exclusion barred the gas station owner's recovery for soil cleanup costs, it did not bar recovery of ground water cleanup costs. *Robert E. Lee Assoc., Inc. v. Peters,* 557 N.W. 2d 457 (Wis. App. 1996). *See also Patz v. St. Paul Fire & Marine Ins. Co.,* 15 F.3d 699 (7th Cir. 1994).

No Coverage under "Personal Injury Coverage"

In *Northbrook Ind. Ins. Co. v. Water District Management Co., Inc*., 892 F.Supp. 170 (S.D. Tex. 1995) the court held that benzene contamination of the District's well water was not a "wrongful entry" covered under the personal injury portion of its CGL policy; otherwise the court held the absolute pollution exclusion would be meaningless. The court cited in support of its holding, *Gregory v. Tennessee Gas Pipeline Co.,* 948 F.2d 203 (5th Cir. 1991) and *Decorative Center of Houston v. Employers Cas. Co.,* 833 S.W.2d 257 (Tex. App.--Corpus Christi 1992, *writ den'd*).

(e) Automobile Injuries. Personal injury or property damage arising out of automobile use.

(f) Property Damage to Other's Property Under Insured's Care. Property damage to property of third parties in the care, custody, and control of the insured.

(g) Assumption of Liability Except Under "Insured Contracts". CGL policies, by endorsement, will extend coverage under the "incidental contract coverage" of the policy to include contractual assumption of liabilities of another person for bodily injury or property damages to a third person ("*Contractual Liability Coverage*" under "*Insured Contracts*").

"Insured contracts" are defined in CGL policies as including "that part of any other contract or agreement pertaining to your business under which you assume the tort liability of another to pay damages because of 'bodily injury' or 'property damage' to a third person or organization, if the contract or agreement is made prior to the 'bodily injury' or 'property damage.'"

"Contractual Liability" coverage is contained in the CGL policy as an exception to an exclusion from coverage. The exclusion provides:

Provision: Contractual Liability Coverage

> This insurance does not apply to "Bodily Injury" or "Property Damage" for which the insured is obligated to pay damages by reason of the assumption liability in a contract or agreement. This exclusion does not apply to liability for damages:
>
> 1. 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; or
>
> 2. that the insured would have in the absence of the contract or agreement.
>
> An "**Insured Contract**" is defined as:
>
> 1. a lease of premises
> 2. a sidetrack agreement
> 3. any easement or license agreement except in connection with construction or demolition operations on or within 50 feet of a railroad
> 4. an obligation, as required by ordinance, to indemnify a municipality, except in connection with work for a municipality
> 5. an elevator maintenance agreement
> 6. that part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work 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.

Contractual Liability coverage excludes coverage for Personal Injury liability assumed by contract or agreement, unless such coverage is endorsed on to the insured's CGL policy. For example, guard service contracts typically contain a provision requiring the owner to indemnify the guard service from liability for the types of liabilities that are embraced by the term "Personal Injury" (libel, slander, defamation of character, false arrest, wrongful eviction, and evasion of privacy). In such case unless the owner has its CGL policy endorsed to cover this indemnity, the owner is uninsured for this contractually assumed liability. Alternatively, the owner could require that it be listed as an additional insured on the guard service's CGL policy.

(5) Duty to Defend. An important coverage under the CGL policy is the "duty to defend" imposed upon the insurer in the event of a suit by an injured or damaged third-party. A typical CGL policy provides that this duty applies "even if the allegations of the suit are groundless, false, or fraudulent." The duty to defend is determined solely from the face of the pleadings and without reference to facts outside the pleadings (sometimes referred to as the "eight corners rule" or the "complaint allegations rule"). *Argonaut Southwest Ins. Co. v. Maupin,* 500 S.W.2d 633, 635-36 (Tex. 1973); *Gulf Chemical & Metallurgical Corp. v. Associated Metals & Minerals Corp.,* 1 F.3d 365 (5th Cir. [Tex.] 1993)-- toxic tort case.

c. Automobile Liability. As noted above, CGL policies exclude coverage for injuries and property damages arising out of use by the Indemnifying Person (including its employees) of an automobile. Depending on the potential risk of the Indemnified Person being named as a defendant in accidents arising out of the Indemnifying Person's use of automobiles, this risk may make it important that the Indemnified Person require the retention of automobile liability coverage.

2. Property Insurance.

a. Landlord and Tenant Relationship. The landlord has an insurable interest in the building. The tenant also has an insurable interest in the building with respect to the leased premises and in the building itself if the tenant has an obligation to repair or rebuild the building in the event of damage or destruction. Both the landlord and the tenant have insurable interests with respect to personal property and fixtures which are located in the building or the leased premises. With respect to improvement installed by the tenant, both the landlord and tenant have insurable interests. The landlord's interest may be insured if the tenant improvements have become fixtures to the building. Likewise, the tenant's interest in the continued use and enjoyment of the tenant improvements is an insurable interest under "improvements and betterments" coverage under its property policy. The tenant will also typically need to obtain insurance for its personal property located at the leased premises, as landlords will typically require a waiver of liability with respect to damage to the tenant's personal property.

The landlord-tenant relationship can range from a single tenant building to a multi-tenant office building.

b. Owner and Contractor Relationship. Property insurance in a construction project is to protect the owner's, contractor's, subcontractor's and lender's economic interests in the project against the project's high vulnerability during construction to the perils of fire, weather, vehicles, equipment, or other named perils.

The number of parties with insurable interests in the project is, thus, more complicated in a construction project than in many other multi- party relationships. The extent of the insurable interests of the two principal parties, the owner and the contractor, depends on whether the construction contract is absolute or divisible. The construction contract determines who bears the risk of loss during the course of construction. If the contractor's obligation is to build a structure for a fixed sum that is absolute and unqualified, the contractor bears the risk of loss before completion of the building. If the owner takes possession of completed portions of the construction in intervals during the course of construction of the entire project, the contract may be characterized as "divisible" with the risk of loss to the completed portions passing to the owner in stages. The subcontractors also have insurable interests in the project to the extent they have provided labor or materials to the project for which payment is not yet made. Therefore, the owner, the contractor, and the subcontractors should be "***named insureds***" and the construction lender should be listed as an "***additional insured***," "***as their interests may appear***."

The most appropriate property coverage during the construction period is "builder's risk insurance." Builder's risk insurance typically protects against damage to or destruction of (1) the building under construction; (2) the contractor's machinery, tools, and equipment at the construction site; and (3) materials and supplies to be used in construction that are at the site or within 100 feet of the site. Builder's risk can either be "named perils" coverage, covering the insured only against losses resulting from specifically named perils (*e.g.*, fire and extended coverage) or "all risk" coverage, covering a broad range of perils with specifically excluded perils negotiated at the time of the purchase of the insurance.

B. "Additional Insured" Status

1. Definition. An "additional insured" is a person covered by an insurance policy in addition to the named insured. The Additional Insured designation seeks to achieve the following "**results**":

(1) **Backstops the Indemnity**. It provides a "safety net" should the indemnity provision be unenforceable or otherwise be deficient.

(2) **Insurance Coverage for the Additional Insured**. It provides a limited form of primary coverage for the additional insured.

(3) **Limits Subrogation Against the Additional Insured**. It may remove the possibility of subrogation against the additional insured for covered liabilities.

(4) **Direct Policy Rights to the Additional Insured**. It provides the additional insured with direct policy rights within the primary insured's policy, including defense cost coverage for claims involving the additional insured.

The Additional Insured designation may involve one or more of the following "**pitfalls**":

(1) **Dilution of Limits Available to the Primary Insured**. The primary insured will be sharing its liability coverage with the additional insured, thereby deleting the total amount of protection available to it.

(2) **Erosion of Limits Available to Additional Insured**. Claims may have already occurred during the policy year, reducing the remaining available Aggregate Limits, thus impairing the limits of liability available to the additional insured through the Additional Insured designation.

(3) **Misleading Certificates of Insurance**. As noted below, when the designation of additional insured status is evidenced only by a certificate of insurance, there is no guarantee of coverage.

(4) **Many Different Forms of Endorsement**. There are many different forms of additional insured designation. It is possible that the additional insured endorsement will be crafted by the insurer to delete the coverage sought by the additional insured. Unless the additional insured stipulates the form of additional insured endorsement, and the choice is left up to the insurer, it is likely that the insurer will provide the most limited form possible.

For a very useful discussion of the "ins" and "outs" of insurance coverage, including copies of the various ISO promulgated Additional Insurance Endorsements, see Comiskey, *Advanced Insurance Issues for Real Estate Attorneys,* ADVANCED REAL ESTATE LAW COURSE v (State Bar of Texas 1996).

2. Types of Insurance.

a. Property. As to property insurance, any person with an "insurable interest" in the insured property can be added as an additional insured.

b. Liability. Additional insured status typically affords the additional insured protection against vicarious liability arising out of the named insured's acts **but depending on the insurance covenant or the policy language** may cover the additional insured's own negligence. As such, it supplements the protection afforded by the indemnity provisions. Richmond, *The Additional Problems of Additional Insureds,* 33 TORT & INS. L. J. 945 (1998); Richmond and Black, *Expanding Liability Coverage: Insured Contracts and Additional Insureds,* 44 DRAKE L. REV. 781 (1996); Sigmier and Reilly, *Coverage for Independent Negligence of Additional Insureds*, FOR THE DEFENSE (Ap. 1995); Beck, *Ethical Issues in Joint Representation Under Subcontract Requirements for Defense and Additional Insured Status*, THE CONSTRUCTION LAWYER 25 (Jan. 1995).

(1) Coverage For Additional Insured's Negligence. For example, listing the owner on the contractor's CGL Policy, or the contractor on its subcontractor's CGL Policy, will afford the owner liability protection. However, whether a covenant to list a person as an additional insured on the insured's liability policy or additional insured status provides coverage for the additional insured's negligence could well depend upon language of the insurance covenant and the insurance policy. When such language is silent or ambiguous, courts may look to the indemnity

language and other language in the contract and custom and practice to determine the intention of the parties. Also, the language of the insurance policy, additional insured endorsement and certificate of insurance will be examined to determine the scope of the insurance coverage.

(a) *Getty* Round 2: Express Negligence Doctrine Not Applicable to Insurance Covenant - Additional Insured's Sole Negligence May Be Covered by Additional Insured Endorsement. In *Getty Oil Co. v. Insurance Co. of North America, NL Industries, Inc., Youell and Companies*, 845 S.W.2d 794 (Tex. 1992), *cert. den'd*, 510 U.S. 820, 114 S. Ct. 76, 126 L. Ed. 2d 45 (1993), the Texas Supreme Court declined to extend the express negligence doctrine to invalidate contractual provisions requiring Getty to be listed as an **additional insured** on NL Industries' liability policies in a case where the indemnity provision excluded indemnity for Getty's negligence **but** the insurance provision did not expressly state that the insurance was to cover injuries due to Getty's negligence. The court reviewed the following provision:

> Seller (NL Industries-the chemical supplier) agrees to maintain at Seller's sole cost and expense, from the time operations are commenced hereunder until Order is fully performed and discharged, insurance of all types and with minimum limits as follows, and furnish certificates to Purchaser's Purchasing Department evidencing such insurance with insurers acceptable to Purchaser (Getty - the chemical buyer):
> ...
>
> | | |
> |---|---|
> | Workmen's Compensation
Statutory Employer's Liability | $500,000 |
> | General Liability:
Bodily Injury | $500,000 |
> | ... | |
> | Automobile Liability:
Bodily Injury | $500,000 |
>
> ...
>
> All insurance coverages carried by Seller, **whether or not required hereby**, shall extend to and **protect** Purchaser, its co- owners and joint venturers (if any), to the full amount of such coverages and shall be sufficiently endorsed to waive any and all claims by the underwriters or insurers against Purchaser, its co-owners, joint venturers, agents, employees and insurance carriers.
>
> Seller shall indemnify, defend and hold harmless Purchaser, its co-owners, joint venturers, agents, employees and insurance carriers from any and all losses, claims, actions, costs, expenses, judgments, subrogations or other damages resulting from injury to any person ... arising out of or incident to the performance of the terms of this Order by Seller ... Seller shall **not** be held responsible for any losses, expenses, claims, subrogations, actions, costs, judgments, or other damages, directly, **solely**, and proximately caused by the negligence of Purchaser. Insurance covering this indemnity agreement shall be provided by Seller. (Emphasis added by author.)

Previously, in a 1986 case ("***Getty* Round 1**"), Getty had been unsuccessful in seeking indemnity against NL Industries. *Getty Oil Corp. v. Duncan*, 721 S.W.2d 475 (Tex. App.--Corpus Christi 1986, *writ ref'd n.r.e.*). Getty lost *Getty* Round 1 when the court determined that the contractual indemnity provision meant what it said: "Seller shall not be responsible for any losses ... solely caused by the negligence of Purchaser."

The facts giving rise to *Getty* Round 1 are as follows. Getty purchased various chemicals from NL Industries for Getty's oil production and exploration operations in the Midland, Texas area. A barrel of chemical demulsifier delivered by NL Industries to Getty exploded in the vicinity of a Getty well, killing Carl Duncan, an independent contractor working for Getty. Duncan's estate and survivors brought wrongful death and survival actions against Getty and NL Industries (*Getty* Round 1). The jury found Getty 100% negligent. The jury also found that NL Industries was not negligent and that it placed adequate warnings on its chemicals. There was, however, no finding that the accident did not arise out of or was not incident to NL Industries' performance of its purchase order.

i) Cause of Action Against Insurance Purchaser for Failure to List Other Party as Additional Insured. The court in the instant action ("***Getty* Round 2**") was being requested by Getty to reverse the holding of the trial court and the court of appeals in a subsequent suit brought by Getty against NL Industries for its failure to name Getty as an "additional insured" on NL Industries' insurance policies and against NL Industries' insurers. Getty was suing on multiple theories: as to NL Industries--breach of contract to purchase insurance on its behalf; violation of § 1.203 of TEX. BUS. & COMM. CODE (Tex. UCC) (Vernon 1994) (obligation of good faith and fair dealing); negligence; violation of the Texas Deceptive Trade Practices Act; and common law fraud; and as to the insurers–breach of contract to extend it insurance coverage; violation of TEX. INS. CODE Art. 3.62 (Vernon 1981) (repealed) (failure to pay claim); breach of the duty of good faith and fair dealing; negligence; violation of the DTPA; and common law fraud.

The trial court in *Getty* Round 2 granted summary judgment against Getty on four grounds: (1) a contract provision requiring the seller to purchase liability insurance for the buyer violated the Texas Oilfield Anti-Indemnity Statute, §§ 127.001-.007, TEX. CIV. PRAC. & REM. CODE ANN. (Vernon 1997); (2) the same contractual provision violated the common law express negligence rule; (3) the prior litigation of a related indemnity provision precluded the present suit under the doctrine of *res judicata* ("*Claim Bar*"); and (4) collateral estoppel prevented Getty from relitigating ultimate issues of fact and law litigated in *Getty* Round 1 ("*Issue Bar*").

The court of appeals sustained the trial court's summary judgment on the basis that Getty was barred by *res judicata*, having already cross- claimed against NL Industries in *Getty* Round 1 for contractual indemnity and having lost. In *dicta*, the court of appeals opined that the insurance provision would

violate the Texas Oilfield Anti-Indemnity Statute by allowing Getty to avoid the consequences of its own negligence. The court of appeals also noted that Texas courts would "undoubtedly extend (the express negligence doctrine) to the insurance provisions covering the indemnity obligation that purport to protect the indemnitee from the results of its sole negligence." 819 S.W.2d 908, 914.

The supreme court found that Getty was not required to bring any of its cross-claims against NL Industries in the suit by Duncan. However, once Getty chose to cross-claim for indemnity, it was required under *res judicata* to bring all its actions in the same action.

ii) Cause of Action Against Insurers. As to the claims against the insurers, the court held that Getty was not barred by either *res judicata* or collateral estoppel. *Res judicata* was not applicable even though as a general matter under Texas law a former judgment bars a second suit against all who were in "privity" with the parties to the first suit. Since NL Industries' insurance policies contained a "no-action" provision (suit against the insurer was specifically prohibited before the insured's liability was reduced to judgment), the court found that Getty could not have joined the insurers as defendants in *Getty* Round 1 anyway. Collateral estoppel did not apply either since the court found that *Getty* Round 2 was not a relitigation of either (1) an issue of fact--did Duncan's injuries arise out of NL's performance of the purchase order? (did the parties intend to limit the insurance to injuries caused by NL Industries' negligence?) or (2) an issue of law--did NL Industries' breach its insurance covenant?

iii) Express Negligence Doctrine Inapplicable. Finally, the court held that the express negligence **doctrine would not be extended** to contractual provisions, other than indemnity agreements, and therefore was not a basis for preventing litigation as to whether Getty was an additional insured under NL Industries' policies. The court stated

> We express no opinion regarding whether Getty is an additional insured under NL's insurance policies with INA or Youell, or the extent of such coverage, if it exists.

Id. 806.

(b) If Express Negligence Standard Not Applicable to Insurance, Is The Clear and Unequivocal Standard Applicable to Insurance Covenants and to Additional Insured Endorsements? Prior to the adoption of the express negligence doctrine as the test to determine whether an indemnity provision extended to the indemnitee's negligence, the Texas Supreme Court followed the "clear and unequivocal" standard. *Fireman's Fund Insurance Co. v. Commercial Standard Indemnity Co.*, 490 S.W.2d 818 (Tex. 1972). See discussion of the *Fireman's Fund* case above at **"IIBlb(1)(b) Indemnity Against One's Own Negligence - Background--1971-1987 Clear and Unequivocal Standard-Broad Statements No Longer Sufficient Unless Obligations Expressed in Clear and Unequivocal Terms-*Fireman's Fund*"**.

i) Insurance Covenant to Obtain Additional Insured Endorsement. Covenants in transaction documents for one party to list the other party and other persons on its liability insurance policies as an additional insured run the gamut from a simple statement "**x shall be listed as an additional insured on Contractor's commercial general liability policy**" to specifying the form of the additional insured endorsement and the relationship between its coverage and the other insurance coverage of the additional insured. The following is an example of a detailed covenant requiring the contractor to list the owner as an additional insured.

Provision:

Paragraph 16.2.2. Commercial General Liability.

Bodily Injury/ combined single limit and umbrella	$1,000,000
Property Damage (Occurrence Basis)	$3,000,000
Products - Comp./Op Agg. $2,000,000	
Personal & Adv. Injury	$1,000,000
Fire Damage (Any one fire)	$100,000
Med. Expense (Any one person)	$5,000

This policy shall be on a form acceptable to Owner, endorsed to include the Indemnified Persons as additional insureds (specifically naming John Doe, John Doe, M.D., P.A. and the Building Owner, and their officers and employees as additional insureds) on standard **ISO form CG 20 26** or other endorsement form acceptable to Owner without exclusion for the additional insured's negligence (whether sole or contributory), contain cross liability and severability of interest endorsements, state that this insurance is primary insurance as regards any other insurance carried by the Indemnified Persons and shall include the following coverages:

1. Premises/Operations;
2. Independent Contractors;
3. Completed Operations for a period of two years following the acceptance of Contractor's Work;
4. Broad Form Contractual Liability specifically in support of, but not limited to, the Indemnity Paragraphs of the contract;
5. Broad Form Property Damage; and
6. Personal Injury Liability with employee and contractual exclusions removed.

Paragraph 16.2.3. Business Automobile Policy.

Bodily Injury - $500,000 combined single limit

This policy shall be on a standard form written to cover all owned, hired and non-owned automobiles. The policy shall include and cover the Indemnified Persons as additional insureds with waiver of subrogation against such persons either by blanket provision in the policy (provided such provision is provided to and reviewed by Owner and determined to be acceptable) or by endorsement by Texas Standard Automobile Endorsement form **TE 99 01B** - Additional Insured and contain a waiver of subrogation in favor of the Indemnified Persons by Texas Standard from **TE 20 46A** - Changes in Transfer of Rights of Recovery Against Others to US (Waiver of Subrogation).

Provisions: *See* the following forms in the Appendix:

1. **Appendix Form 8 Attachment to Contractor's Certificate or Proof of Insurance**.

2. **Appendix 14 ISO form CG 20 26. 11 85 Additional Insured - Designated Person or Organization.**

3. **Appendix 20 CGL Blanket Endorsement. Contractor's Extended Liability.**

4. **Appendix 10 TE 99 01B - Additional Insured**.

(ii) Scope of Additional Insured Endorsement. The scope of coverage of an additional insured endorsement is defined by the words of the policy and the endorsement to the policy. The Insurance Services Office, Inc. ("*ISO*"), a trade organization to which most national insurers belong, has promulgated numerous additional insured endorsements for use nationally.

Provisions:

See **Footnote [45]** to Volume 2 of this Article for a **List of ISO Additional Insured Endorsements** for a listing of these commonly used endorsements. *See* the following most commonly used additional insured endorsement forms in the Appendix:

Commercial General Liability Policies:

1. **Appendix 13 CG 20 10 10 91 Additional Insured-Owners, Lessees or Contractors-Scheduled Person or Organization**.

2. **Appendix 14 CG 20 26 11 85 Additional Insured- Designated Person or Organization**.

3. **Appendix 15 CG 20 11 01 96 Additional Insured-Managers or Lessors of Premises**.

4. **Appendix 21 CG 20 33 07 98 Additional Insured-Owners, Lessees or Contractors–Automatic Status When Required in Construction Agreement with You.**

5. **Appendix 22 CG 20 37 10 01 Additional Insured-Owners, Lessees or Contractors–Completed Operations.**

Business Auto Policies: The omnibus "**who is the insured**" clause of the basic standard Business Auto Policy ("***BAP***") automatically includes the most common circumstances in which parties other than the named insured are insured under the named insured's policy.

1. **CA 00 01 07 97 Business Auto Policy Omnibus Insured Provision.** This form of BAP covers within the "who is the insured" and the "you" references: the named insured; various persons using a covered auto owned, hired, or borrowed by the named insured with the named's insured's permission (the "permissive user" category of insureds); and any person liable for the conduct of an insured "to the extent of that liability."

2. **Appendix 10 TE 99 01 B Additional Insured Endorsement.** This form has been approved for use in Texas to the same effect as the CA 2048. In addition to specifying insured status for a person named in the endorsement, the Texas endorsement also provides notice to the additional insured when the policy is cancelled.

3. **Appendix 11 TE 20 46 A** - Changes in Transfer of Rights of Recovery Against Others to US (Waiver of Subrogation).

Workers Compensation. It is not generally appropriate (except in borrowed servant, dual employment or leased employee situations) for one party to a contract to require the other party to name the other party as an additional insured on its workers compensation and employers liability policy. This would result in the other party being covered for injuries to its employees under the insured's worker's compensation policy. As discussed elsewhere in this Article, the concern raised by the risk of third-party actions by an injured employee of an insured employer against a related party (*e.g,* suit by an injured employee of a contractor against the premises owner, or suit by an injured employee of a subcontractor against the contractor, or suit by an injured employee of a tenant against the landlord) can be addressed by indemnification by the employer and designation of the related party as an additional insured.

Appendix 12 WC 42 03 04A Waiver of Our Right to Recover from Others. The additional concern that the workers compensation carrier will seek reimbursement from a party liable for the employee's injury (other than the employer against whom such suits are barred) may be addressed by contractually requiring the employer/indemnifying person to waive rights of subrogation.

A Houston Court of Appeals held that the insurance covenant to obtain an additional insured endorsement reviewed by the court did not evidence an intent to cover the sole negligence of an additional insured. In *Emery Air Freight Corp. v. General Transport Systems, Inc.*, 933 S.W.2d 312 (Tex. App.--Houston [14th Dist.] 1996, *no writ*], the court found that the following additional insured provision did **not** cover a liability that arose out of the sole negligence of the additional insured:

Provision:

> 7. Contractor shall obtain and maintain at its own expense insurance in such forms and minimum amounts as set forth below naming Emery as an additional insured. Contractor shall furnish Emery certificates from all insurance carriers showing the dates of expiration, limits of liability thereunder and providing that said insurance will not be modified on less than thirty (30) days' prior written notice to Emery.
>
> Minimum Limits of Insurance:
>
> A. Worker's Compensation -- Statutory
> B. General Liability Insurance -- $1 Million Combined Single Limit
> C. Automobile Liability -- $1 Million Combined Single Limit
>
> If Contractor fails to obtain and maintain the insurance coverage set forth above, Emery shall have the right, but not the obligation, to obtain and maintain such insurance at Contractor's cost or, at its option, to terminate this Agreement for cause as provided in Section 9 hereof.
>
> 8. Contractor shall be solely responsible and liable for any and all loss, damage or injury of any kind or nature whatever to all persons, whether employees or otherwise, and to all property, including Emery shipments while in the Contractor's custody and control, arising out of or in any way resulting from the provision of services hereunder, and Contractor agrees to defend, indemnify and hold harmless Emery, its agents, servants, and employees from and against any and all loss and expense, including legal costs, arising out of the provision of the services hereunder, by Contractor.

This provision was contained in a Cartage Agreement, an agreement whereby GTS agreed to provide local delivery services in Beaumont for Emery, a national freight service. Apparently, the Beaumont facility from which GTS provided the delivery service was "owned or operated" by Emery, but the Cartage Agreement provided that GTS had exclusive charge and control of the services being performed. *See* footnote 1 in the opinion. The trial court however determined that Emery was solely liable for the injury sustained by one of GTS's employees at the Beaumont facility. This suit was brought by Emery against GTS to reimburse Emery for the monies awarded to the injured employee. Emery sought to recover against GTS for failing to cause GTS's liability insurance to list Emery as an additional insured.

The court of appeals noted that the Texas Supreme Court had twice previously, in *Getty Oil Co. v. Insurance Co. of North America* (*Getty II* discussed immediately above) and *Fireman's Fund Ins. Co. v. Commercial Standard Ins. Co.* (discussed previously), dealt with the interaction of an indemnity clause and an insurance clause in a contract. The Fireman's Fund contract had a liability insurance clause which required the contractor to obtain liability insurance in order to "**protect** the Owner ... against all liabilities, claims, or demands for injuries or damages to any person or property growing out of the performance of work under this specification." *Fireman's Fund,* 490 S.W.2d at 821. Another clause, appearing later in the contract, indemnified the owner from claims arising from the contractor's performance (with the exception of those claims arising out of the owner's negligence). The *Fireman's Fund* court addressed whether the language of the insurance clause reflected an intention for the contractor to carry insurance covering the owner's negligent acts. The court noted that the above-quoted language from the insurance clause was "**insufficient to clearly** indicate an intention to protect the contractor-indemnitee against liability for damages caused solely by the latter's (the owner's) own negligence." *Id.* at 822. Noting that "all of the relevant provisions of a contract should be considered in arriving at its intent and meaning," the *Fireman's Fund* court observed that other sentences in the insurance provision required liability insurance covering only the contractor's agents, employees, and vehicles. It also noted that the indemnity provision specifically excepted any assumption of the owner's negligence by the contractor. The *Fireman's Fund* court held that

> (W)e cannot agree ... that the requirement in Section 12 that Wallace carry certain liability insurance for the protection of General Motors evidenced an intention to cover negligent acts of the latter. While the meaning of the contract provisions relating to liability insurance are not clear, the most reasonable construction is that they were to **assure performance of the indemnification agreement** as entered into by the parties. Such provisions are often required to guard against the insolvency of the indemnitor, and they should not be considered as evidence of intent to broaden the contractual indemnity obligation.

Fireman's Fund, 490 S.W.2d 818, 823 (Tex. 1972).

The court of appeals in *Emery* noted that the Texas Supreme Court in *Getty* had determined that the additional insured provision being litigated in *Getty* was a free-standing obligation, which required by its language an extension of coverage "whether or not required [by the other provisions of the contract]" and was in addition to the requirement in the indemnity provision that contained an internal provision for insurance to support the indemnity. *Getty*, at 804, 806.

The court of appeals noted that the supreme court in *Getty* declined to extend the express negligence rule to insurance agreements, and concluded that

> As such, an insurance agreement which stands alone can shift the risk of insuring against one party's own negligence to another party without a specific

> expression of intent, even though an indemnity clause cannot.
>
> This case, then, requires a **two-step analysis**. First, we must determine whether the indemnity clause satisfies the express negligence rule, thereby indemnifying appellant (Emery) against its own negligence. Second, we must determine whether the insurance clause merely supports the indemnity clause or stands alone, representing an independent obligation.

The court of appeals held that even though Emery was to be listed as an additional insured on GTS's liability insurance policy, the "'most reasonable construction' of the insurance provisions in the Cartage Agreement 'is that they were to assure the performance of the indemnity agreement as entered into by the parties.'" [The court borrowed such language from the court in *Fireman's Fund*]. The court based this determination on the following **factors**:

(1) the indemnity provision did not have an internal provision requiring insurance to support the indemnity distinct from other provisions for insurance in the agreement;

(2) the insurance provision does not require coverage "whether or not required" by other clauses; and

(3) the insurance clause does not **expressly cover negligence**, nor did the indemnity clause, because of the application of the express negligence rule.

Another court of appeals has found that the "additional insured" endorsement to a CGL did **not** cover the negligence of the additional insured, but only the negligence of the "first named insured" (the contractor). ***Granite Construction Co., Inc. v. Bituminous Ins. Cos.,*** 832 S.W.2d 427 (Tex.App.--Amarillo 1992, *no writ*). Granite sought coverage for a lawsuit brought by an employee of a contractor hired by Granite to haul asphalt from its construction site. Granite had agreed by contract to load the trucks and the contractor's responsibility was to haul the asphalt after Granite loaded the trucks. Granite was named as an "additional insured" in the contractor's CGL policy. The endorsement limited Granite's coverage as follows:

Provision:

> Liability arising out of **operations** performed for such insured (Granite) by or on behalf of the named insured (the contractor).

In the negligence suit the employee alleged that Granite had negligently loaded its truck in such a manner that the truck overturned and injured him. Granite sought coverage under the additional insured endorsement, contending that the employee's injuries "arose out of" hauling operations performed for Granite by the contractor. The court disagreed, holding that the claim against Granite arose out of Granite's loading operations and not out of operations performed by the contractor, the only operations for which Granite was insured. *Id.,* 430. The court also rejected Granite's argument that the employee's claim was covered because of the certificate of insurance naming it as an insured for all of its work in Texas. The court held that the certificate itself did not manifest the coverage afforded Granite, rather it merely evidenced Granite's status as an insured. *Id.,* at 429.

The Texas Supreme Court has recently given a broad construction to the phrase "**arising out of***"* in a case involving the construction of an automobile policy. In *Mid-Century Ins. Co. v. Lindsey,* 997 S.W.2d 153, 156 (Tex. 1999), while attempting to get into his parents' truck through the sliding rear window, a boy accidently touched a loaded shotgun on a gun rack mounted over the window and shot a man sitting in an adjacent parked car. The relevant insurance policy provided coverage for injuries *arising out of* the use of a motor vehicle. The court held:

> For liability to "**arise out of**" the use of a motor vehicle, a **causal connection** or **relation** must exist between the accident or injury and the use of the motor vehicle.

Id. at 156. While the direct cause of the injury stemmed from the boy's conduct in touching the gun, the court concluded that the man's injury "arose out of" the use of the truck because the injury-producing act and its purpose were an integral part of the use of the vehicle. *Id.* at 158- 59. The court noted that the vehicle must be more than the "locational setting" for the injury. *See id.* at 156.

The First Court of Appeals considered "***arising out of***" in the context of an additional-insured provision covering liabilities arising out of the "***operations***" of the named insured in ***Admiral Ins. Co. v. Trident NGL, Inc.***, 988 S.W.2d 451 (Tex.App. [1st Dist.] 1999, *writ den'd*). In *Admiral*, a company hired to service an oil and gas facility named the facility's owner as an additional insured for liability arising out of the service company's "operations." While one of the service company's (the named insured's) employees was unloading tools on the premises of the additional insured, a compressor on the property exploded. The employee, injured as a result of the explosion, sued the facility's owner, and the owner sought a declaration that he was covered as an additional insured under the policy. The court of appeals followed what it considered the "majority view" from federal courts and courts in other jurisdictions construing similar endorsements:

> [F]or liability to "*arise out of* **operations**" of a named insured it is not necessary for the named insured's acts to have "caused" the accident; rather it is sufficient that the named insured's employee was injured while present at the scene in connection with performing the named insured's business, even if the cause of the injury was the negligence of the additional insured. (emphasis added)

The Third Court of Appeals has also found that an additional insured's negligence is covered by an additional insured endorsement covering liabilities "*arising out of [the named insured's]* ***work***" in ***McCarthy v. Cont. Lloyds,*** 7 S.W.3d 725 (Tex. App.-Austin [3rd Dist.] 1999, *no writ*). McCarthy, a general contractor, hired Crouch/Fisk Electric Company and Crouch Electric Company to provide electrical

services for a Motorola construction project McCarthy was managing. An employee of Crouch (the named insured) was injured as he walked down a slippery incline on premises owned by McCarthy (the additional insured). Walking down the incline to get tools to perform Crouch's work was an integral part of its work of McCarthy. Crouch/Fisk and Crouch Electric purchased separate commercial general liability insurance policies from Continental Lloyds Insurance Company ("CLIC") and American Casualty Company of Reading, Pennsylvania ("ACC"). McCarthy was added to both policies by endorsement as an additional insured. The additional insured endorsements read as follows:

Provisions:

CLIC Additional Insured Endorsement

WHO IS AN INSURED ... the person or organization shown in the Schedule (McCarthy), but only with respect to liability *arising out of* "**your work**" (Crouch's) for that insured (McCarthy) by or for you (Crouch). [emphasis added]

ACC Additional Insured Endorsement

The insurance provided to the additional insured is limited as follows: 1. That person or organization [McCarthy] is only an additional insured with respect to liability *arising out of*: ... b. "**Your work**" for that additional insured (McCarthy) by or for you (Crouch). [emphasis added]

The insurance companies argued that "arising out of" means coming *directly* from the negligence of Crouch, the contractor, and could not arise in a case where only the owner was negligent. The court of appeals found that **coverage** occurs where there is a **causal connection** between the liability and the named insured's work, even though only the additional insured is negligent. The employee's injury occurred while he was on the construction site for the purpose of carrying out Crouch's work for McCarthy. Thus, there was a causal connection between the injury and Crouch's performance of its work for McCarthy; accordingly, McCarthy's liability for the injury "arose out of" Crouch's work form McCarthy. The court noted

> As he was walking down this incline to go to the equipment trailer, Wilson 'fell on the muddy, slippery surface.' These allegations show that walking down the incline to get tools to perform its job was an integral part of Crouch's work for McCarthy. Thus, the accident occurred while Wilson was on the construction site for the purpose of carrying out Crouch's contract with McCarthy. There was more than a mere locational relationship between the injury and Wilson's presence on the site. Wilson's injury occurred while he was carrying out a necessary part of his job for Crouch. Therefore, there is a **causal connection** between Wilson's injury and Crouch's performance of its work for McCarthy and the liability "arose out of" Crouch's work for McCarthy.

The court rejected the insurance company's attempt to limit coverage to cases where the named insured also was negligent. The court held

> The insurance companies offer a competing interpretation for the phrase "arising out of" that they claim is equally reasonable and thus creates an ambiguity. Their interpretation would limit the interpretation of "arising out of" to mean coming ***directly*** from; *i.e.*, for liability to arise out of Crouch's work for McCarthy, the liability must stem *directly* from Crouch's negligence and cannot extend to negligence caused solely by McCarthy. Post-*Lindsey*, however, such a restrictive interpretation no longer appears reasonable in Texas and cannot be used to create ambiguity. However, were we to consider the phrase "arising out of" ambiguous, we would apply the familiar rules that construe the policy against the insurer and reach the same result.

The court of appeals in ***Highland Park v. Trinity Universal Ins. Co.,*** 36 S.W.3d 916 (Ct.App. [5th Dist.] Dallas, 2001, *no writ*) also was called upon to construe an "arising out of 'your **work**'" additional insured provision. James Watkins, a plumber employed by Ward Brothers, was injured on the Highland Park Shopping Center premises owned by Henry S. Miller Interests, Inc. while riding a Man-Lift in Highland Park's parking garage. Trinity Universal refused to defend Highland Park in the suit brought by Watkins in which he alleged that the Man-Lift was unsafe. Based on *McCarthy* and *Trident NGL*, the court found that the additional insured endorsement **covered** Highland Park's sole negligence because the liability arose out of the work of the named insured on the additional insured's premises.

The Fifth Circuit applying Texas law followed *Trident NGL* as opposed to *Granite* in ***Mid-Continent Casualty Co. v. Swift Energy Co.,*** 206 F.3d 487 (5th Cir. 2000). This case involved two contractors (Air Equipment and Flournoy Drilling Co.) performing services for the same party (Swift Energy Co.). Air Equipment was both a contractor of Swift Energy and a contractor performing services for Flournoy. Air Equipment's employee (Lozano) was injured on Swift Energy's well site while performing services for Flournoy. Swift Energy was an additional insured on Air Equipment's liability policy pursuant to the following policy provision that designated as additional insured persons

Provision:

> **SCHEDULE. Name of person or organization:**
>
> Any person or organization for whom the named insured has agreed by written "insured contract" to designate as an additional insured subject to all provisions and limitations of this policy....
>
> WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability *arising out of your* ***ongoing operations*** performed for that insured. (emphasis added)

The contract between Swift Energy and Air Equipment contained a mutual indemnity provision, required each party to carry liability insurance to support the indemnified liability under each party's indemnity, and

required each party to add the other to its liability policy "for liabilities and indemnities assumed by" the indemnifying party. Mid-Continent argued that Air Equipment's employee was injured while performing work for Flournoy and not for Swift and therefore although Swift was an additional insured under Air Equipment's policy, the injury was not a liability covered by Air Equipment's indemnity to Swift and consequently was not a liability covered pursuant to the "insured contract" provisions of Air Equipment's policy with respect to Swift's additional insured status thereunder. Mid-Continent also argued that the indemnity contract between Air Equipment and Swift was unenforceable under the Texas Oilfield Anti-Indemnity Act ("*TOAIA*") on various grounds. TEX. CIV. PRAC. § REM. CODE ANN. § 127.003 (Vernon 1997).

The court reject Mid-Continent's arguments finding that Mid-Continent asked the wrong question.

> We emphasize that Mid-Continent's first argument does not require us to determine whether Swift was entitled to indemnity under the indemnity provision of the MSA (the contract between Swift and Air Equipment). Rather, it requires us to answer the different question of whether Swift should be denied coverage as an additional insured under the Policy because the MSA is not an "insured contract." The presumptions involved in these different contexts are diametrically opposed. .... under Texas law indemnity agreements are strictly construed in favor of the indemnitor (here, Air Equipment).... By contrast, insurance policies are strictly construed in favor of **coverage** (for Swift)....It does appear that Lozano was injured while on Swift's premises for the purpose of helping to perform Air Equipment's business. This is the exact factual scenario present in *Admiral.* In sum, while we are not required to decide whether *Granite* and *Admiral* are distinguishable, if they are, *Admiral* would govern under these facts.

The court also reasoned that even if the liability arose out of Air Equipment's operations for Flournoy, they also arose out of Air Equipment's operations for Swift, since Flournoy was Swift's contractor.

The Fifth Circuit in *Mid-Continent Casualty Co. v. Chevron Pipe Line*, ___ F.3d ___ (5th Cir. 2000) construed an "arising out of your **work**" additional insured endorsement as **covering** injuries to a named insured's employee performing services for the additional insured on the additional insured's premises. The court noted

> The Mid-Continent endorsement and those in *Granite* and *Admiral* are *not* identical. Mid-Continent uses "liability arising out of 'your (PMI's) ***work***'", defined by the policy as the named insured's [PMI's] work *or* operations, while the *Granite* and *Admiral* endorsements, respectively, used "liability arising out of ***operations*** performed ... by or on behalf of the named insured", ... and "liability arising out of the named insured's operations" *Admiral,* 988 S.W.2d at 454 (emphasis added). On the other hand, the pertinent language in the two additional insured endorsements at issue in *McCarthy* is identical to that in Mid-Continent's. *See McCarthy*, 7 S.W.3d at 727 n. 4. .... To the extent that there is a conflict in the approach taken by *Granite* and *Admiral* in interpreting the endorsement, *e.g.,* fault-based versus activity-based, we agree with CPL that our affirming the coverage-for-CPL-ruling does *not* require us to resolve such conflict. We are persuaded that, in the light of *Granite's* focus on the word "*operations*" in the endorsement, which it considered in conjunction with the parties' division of operations in its services contract, there is *no* need here to reach the same non-coverage holding. First, the word "operations" does *not* appear in the Mid-Continent endorsement; rather, it uses "your **work**", which, per its policy definition as *work or operations*, may indicate that broader coverage was intended; second, the underlying services contract does *not* divide responsibilities between CPL and PMI *vis-a-vis* PMI's work; and finally, based on the finding in the *Fant* action that PMI controlled Fant's work at CPL, his injury, at least in part, "arose out of" PMI's work for CPL. [Emphasis added]

Majority Rule: Out of State

Cases Finding Coverage of Additional Insured's Negligence. The following cases have upheld coverage of an additional insured's negligence: *Marathon Ashland Pipe Line v. Maryland Casualty*, 243 F.3d 1232 (10th Cir. 2001)(under Wyoming law "ongoing operations for insured" type additional insured endorsement covers the "natural consequence" of the named insured's act hiring its employee and includes the negligence of the additional insured; court noted that WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY (Unabridged 2000) at page 1576 defines "***ongoing***" as "that [which] is going on; that [which] is actually in progress: and at page 1581 defines "***operations***" as "a doing or performing esp[ecially] of action); *Fireman's Fund Ins. Co. v. Atlantic Richfield Co.,*____(Cal.App. 4th 2001)(finding that **ISO CG 20 10 10 01 Additional Insured-Owners, Lessee or Contractors (See Appendix 13)** which covers an additional insured for liabilities arising out of the work of the named insured covered the additional insured's sole negligence [failure to maintain a step] because the accident happened while the injured employee was performing work for the additional insured); *Meadow Valley Contractors v. Transcontinental Ins. Co.,* 27 P.3d 594 (UT 2001)("liability arising out of your work" endorsement covered additional insured's sole negligence since it "originated from, was incident to, and was in connection with" the work of the named insured); *Philadelphia Electric Co. v. Nationwide Mutual Ins. Co.*, 721 F.Supp. 740 (E.D. PA. 1989)-found additional insured endorsement for "any work performed by (insured)" as broad enough to cover additional insured's negligence (indemnity was generally worded indemnity with exclusion for indemnitee's sole negligence); *Rupp v. American Crystal Sugar Co.,* 465 N.W.2d 614, 617 (N.D. 1991)-court held "there could be no purpose for the insurance provision other than to protect (the owner) from the consequences of its own negligent acts"; *Clark v. B & D Inspection Service*, 896 F.2d 105 (5th Cir. 1990)-construed the following policy language: "as an additional insured, any person or organization when required to be so named but only as

respects operations of the named insured" as including additional insured's negligence finding that "the policy language addresses the factual context in which the liability of the named insured arises, not the legal theory on which it is based."; *Woods v. Dravo Basic Materials Co.,* 887 F.2d 618 (5th Cir. 1989)-insurance covenant to "cover all risks"; *Valentine v. Aetna Ins. Co.,* 564 F.2d 292 (9th Cir. 1977); *Jokich v. Union Oil Co.,* 574 N.E.2d 214 (Ill. 1991)-insurance covenant provided that it was not limited by the coverage of the indemnity (indemnity provision was a limited indemnity excluding the Indemnified Person's sole negligence); *McIntosh v. Scottsdale Ins. Co.,* 992 F.2d 251 (10th Cir. 1993); *Saavedra v. Murphy Oil U.S.A., Inc.,* 93 F.2d 1104 (5th Cir. 1991); *Charter Oak Fire Ins. C. v. Trustees of Columbia University*, 604 N.Y.S.2d 55 (1993); and *Transamerica Ins. Group v. Turner Constr. Co.,* 601 N.E.2d 473 (1992).

Minority Rule: Out-of-State Cases Finding Additional Insured Not Covered for Own Negligence. *Consolidation Coal Co. v. Liberty Mutual Ins. Co.,* 406 F.Supp 1292 (W.D.Pa. 1976)-insurance covenant limited additional insured's coverage to "but only with respect to acts or omissions of the named insured in connection with the named insured's operations"; *First Ins. Co. v. State,* 665 P.2d 648 (Ha. 1983)-additional insured endorsement contained an exclusion of coverage for "...bodily injury or property damage arising out of any act or omission of the additional insured or any of his employees, other than general supervision of work performed for the additional insured by the named insured"; *National Union Fire Ins. Co. v. Glenview Park District,* 632 N.E.2d 1039 (Ill. 1994)-policy provided coverage "...with respect to operations performed by or on behalf of the Named Insured" but then stated that the coverage "... shall not apply to damages arising out of the negligence of the Additional Insured(s)..."

A number of courts have held that the "additional insured" is only covered for liability resulting from the negligence of the named insured (*i.e.,* only for vicarious liability), and not the additional insured's own negligence. *Harbor Ins. Co. v. Lewis,* 562 F.Supp. 800 (E.D. Pa. 1983); *Travelers Ind. Co. v. Hanover Ins. Co.,* 470 F.Supp. 630 (E.D. Va. 1979); *National Union Fire Ins. Co. v. Glenview Park District,* 632 N.E.2d 1039 (1994); *Federal Ins. Co. v. Commerce & Industry Ins. Co.,* 589 N.Y.S.2d 439, 187 A.D.2d 278 (1992), *appeal den'd,* 599 N.Y.S.2d 804, 616 N.E.2d 159 (1993); *Scottish & York Int'l Ins. Group v. Ensign Ins. Co.,* 709 P.2d 397 (Wash. App. 1985).

(2) Exclusion if Additional Insured Has Insurance. The decision in *Elf Exploration, Inc. v. Cameron Offshore Boats, Inc*., 863 F. Supp. 386 (E.D. Tex. 1994) also illustrates the risk inherent in not reading the insurance policy of the party obligated to name the prospective additional insured as an additional insured. The court found that a fact issue existed defeating a summary judgment motion as to whether the proposed additional insured had accepted the defendant's insurance policy which contained an additional insured provision that included the plaintiff, but which provision was worded so as to exclude coverage in cases where the proposed additional insured was already insured (a so-called "***Escape Clause***").

Provision:

> Provided that where the Assured is, irrespective of this insurance, covered or protected against any loss or claim which would otherwise have been paid by the Assurer, under this policy, there shall be no contribution by the Assurer on the basis of double insurance or otherwise.

The party providing the insurance provided insurance naming the proposed additional insured as an additional insured and therefore did not violate the covenant to name the plaintiff as an additional insured, but the additional insured provision contained as Escape Clause. Timely review and objection may need to occur to defeat this waiver argument!

(3) Express Exclusion of Additional Insured's Negligence. The holding in *BP Chemicals, Inc. v. First State Ins. Co.,* 226 F.3d 420 (6th Cir. 2000) in which the 6th Circuit applied Texas law emphasizes why it is important to obtain and read a copy of the Additional Insured Endorsement and not to rely either upon a statement in the Certificate of Insurance that "'x' is an additional insured for liabilities arising out of the work 'y'" or upon a general statement in the contract that "x" is to be listed as an additional insured on "y's" commercial general liability policy. The court in this case held that the additional insured endorsement meant exactly what it said "the negligence of the additional insured is excluded" and that the certificate of insurance stating that "x" was an additional insured and the contractual provision in the contract between "x" and "y" that be listed as an additional insured did not clearly provide for coverage of the additional insured's negligence. The following are the provisions in the contract, the certificate of insurance and the endorsement.

Provisions.

> **Contract.** Contractor [Bath] shall have a comprehensive general liability policy in the amount of at least $1,000,000 with an Additional Insured Endorsement naming Owner [BP Chemical] as an additional insured.
>
> Contractor hereby indemnifies and agrees to defend and save Owner and its affiliated Corporations, their agents, servants and employees harmless from any and all losses, expenses, demands and claims that may be claimed or for which suit is brought for any actual or alleged bodily injury or death occurring to any person whatsoever, in any manner arising out of or in connection with, or resulting in whole or in part out of the acts of omissions of Contractor, or any subcontractors employed by or under the direct control of the Contractor, and their respective officers, agents and employees in the performance of the Work in accordance with this Agreement, and agrees to pay all damages, costs and expenses, including attorneys' fees, arising in connection therewith. Such obligation shall not apply when the liability arises solely from the negligence of Owner, its employees or agents. Such obligation shall also be limited, in a case involving or alleging joint negligence between Contractor and Owner, its employees or agents, to Contractor's actual

percentage of comparative negligence, if any, found by the trier of fact in a cause of action brought against Contractor arising out of the performance of the Work or alleged negligence in accordance with this Agreement. This indemnity obligation of Contractor shall not be applicable to the extent that Owner is provided coverage as an additional insured under Contractor's insurance policies as specified in Exhibit A to this Contract, or to the extent that the right of indemnity is prohibited or limited by the laws of the state in which the Work is located.

Certificate of Insurance. Owner is an additional insured thereunder as respects liability arising out of or from the Work performed by Contractor for Owner.

Endorsement. It is agreed that additional insureds are covered under this policy as required by written contract, but only with respect to liabilities arising out of their operations performed by or for the named insured, **but excluding any negligent acts committed by such additional insureds**.

(4) Listing as Additional Insured Without Indemnity Agreement. There are important considerations to be remembered when evaluating relying solely upon listing a party as an additional insured without a backup contractual indemnity agreement. The policy may be canceled with or without the additional insured's knowledge; the insurer may become insolvent; and policy limits and exclusions from coverage may limit the protection.

(5) Cause of Action Against Insurance Purchaser for Failure to List Other Party as Additional Insured. A party that breaches its contractual obligation to list the other party as an additional insured is liable for all damages suffered as a result by the non-listed party, including attorney's fees incurred by the non-listed party in defending a claim that would have fallen within the protection of the additional insured endorsement. The court in *Coastal Transport Co. v. Crown Central Petroleum Corp*., 20 S.W.3d. 119 (Tex.App.-Houston [14th Dist.] 2000, *writ denied*) found that Coastal failed to list Crown as an additional insured on Coastal's Trucker's Policy and was liable to Crown for the $4,816,549.28 judgment obtained by an employee of Coastal that was injured on Crown's premises. Crown was sued by Coastal's employee, who was injured when the truck he was refueling on Crown's premises caught fire due to Crown's negligent maintenance of Crown's gas refueling equipment. The insurance provision did not refer to an additional insured designation but provided for Coastal to obtain insurance protecting Crown.

Provision:

Carrier agrees to purchase at Carrier's cost ... Comprehensive General Liability Insurance including care, custody and control coverage and liability assumed with $1,000,000 limit per occurrence for bodily injury and property damage combined.

(6) Additional Insured's "Other Insurance". The use of additional insured status as a risk transfer device is aimed at procuring insurance protection under someone else's policy rather than having to rely upon on one's own policy. Additional insured Indemnified Person's must verify that any **other insurance coverage** to which they have access will not interfere with payment by the Indemnifying Person's policy on a primary and non-contributory basis. This is the interplay of the Indemnifying Person's CGL policy with the additional insured's own CGL policy.

Assuming both the Indemnifying Person's CGL policy and the additional insured/Indemnified Person's policies are standard from policies, then both will declare themselves to be **primary** insurance **unless** some modification is effected to eliminate this conflict by amendment to the Indemnified Person's policy. *Hardware Dealers Mutual Fire Ins. Co. v. Farmers Ins. Exchange,* 444 S.W.2d 583 (Tex. 1969). Note that endorsing the Indemnifying Person's policy to provide that it is primary does not solve the problem. In fact, most CGL policies already provide that they are primary in virtually all cases in which the additional insured would bring a claim on that CGL policy. But the policy also provides for **proration** when other insurance is available to the additional insured. *Hardware Dealers Mutual Fire Ins. Co. v. Farmers Ins. Exchange,* 444 S.W.2d 583 (Tex. 1969).

The following is the standard "other insurance" provisions in the ISO standard CGL policy form:

3. Other Insurance.

If other valid and collectible insurance is available to the insured for a loss we cover under Coverages A or B of this Coverage Part, our obligations are limited as follows:

a. Primary Insurance

This insurance is primary except when b. below applies. If this insurance is primary, our obligations are not affected unless any of the other insurance is also primary. Then we will share with all that other insurance by the method described in c. below.

b. Excess Insurance

This insurance is excess over any of the other insurance, whether primary, excess, contingent or on any other basis:

(1) That is Fire, Extended Coverage, Builders Risk, Installation Risk or similar coverage for "your work;"

(2) That is Fire insurance for premises rented to you; or

(3) If the loss arises out of the maintenance or use of aircraft, "autos" or watercraft to the extent not subject to Exclusion g. of Coverage A (Section 1)

When this insurance is excess, we will have no duty under Coverages A or B to

defend any claim or "suit" that any other insurer has a duty to defend. If no other insurer defends, we will undertake to do so, but we will be entitled to the insured's rights against all those other insurers.

When this insurance is excess over other insurance, we will pay only our share of the amount of the loss, if any, that exceeds the sum of:

(1) The total amount that all such other insurance would pay for the loss in the absence of this insurance; and

(2) The total of all deductible and self-insured amounts under all that other insurance.

We will share the remaining loss, if any, with any other insurance that is not described in this Excess Insurance provision and was not bought specifically to apply in excess of the Limits of Insurance shown in the Declarations of this Coverage Part.

c. Method of Sharing

If all the other insurance permits contribution by equal shares, we will follow this method also. Under this approach each insurer contributes equal amounts until it has paid its applicable limit of insurance or none of the loss remains, whichever comes first.

If any of the other insurance does not permit contribution by equal shares, we will contribute by limits. Under this method, each insurer's share is based on the ratio of its applicable limit of insurance to the total applicable limits of insurance of al insurers.

The additional insured/Indemnified Person should amend its own policy to provide that it is **excess coverage** to the insurance available to it as an additional insured under the Indemnifying Person's CGL policy. One commentator has suggested that the way of addressing this "pitfall" is to request a "**Primary Liability Endorsement**" to the primary insuring party's policy. *See* Comiskey, *Advanced Insurance Issues for Real Estate Attorneys,* ADVANCED REAL ESTATE LAW COURSE v-4 (State Bar of Texas 1996) which offers the following advice:

> The purpose is to eliminate the effects of the "Other Insurance" clause, preventing one insured's liability insurance from participating in sharing a loss with a liability insurance of another insured. Be forewarned, however, that there is no standard form of Primary Liability wording, and many insurance will not offer primary liability coverage. When confronted with a insurance company that is unwilling to provide this endorsement, a reasonable compromise is to request that Primary Liability be **provided at least for the scope of the Additional Insured endorsement**. Then be certain that you have requested the broadest possible Additional Insured wording. Outside of Texas, it is a fairly common practice for the Additional Insured to **endorse that organization's policy to be excess over the Primary Liability insurance**. That is a valuable safeguard. The Texas Department of Insurance, however, does not recognize this endorsement, and many insurance companies are therefore not familiar with this opportunity.
>
> *See* **Appendices 17-18** for "Other Insurance" Clauses and ISO Endorsements to Indemnitee's CGL Policy.

3. Persons Listed. A disadvantage of being an "additional insured" as opposed to a "named insured" is that additional insured status does not provide coverage for the officers, directors, and partners of the additional insured, unless specifically listed individually as additional insureds. An additional insured provision covering "employees" of the additional insured does not cover a "volunteer" assisting the additional insured. ***Sturgill v. Kubosh Ins. Co. of America***, __ S.W.2d __ (Tex. App.- -Houston [1st Dist.] Nov. 14, 1996) 1996 WL 665552.

4. Oilfield Anti-Indemnity Statute Not Prohibitive of Additional Insureds Covenant. In *Getty*, the Texas Supreme Court additionally held that the Texas Oilfield Anti-Indemnity statute did not prohibit an insurance covenant requiring a person (in this case the "Indemnified Person") from being listed as an additional insured on the Indemnifying Person's liability insurance policies. The insurers argued that the practical effect of contracting for an additional insured provision in the contract between Getty and NL Industries was to cause Getty to be indemnified for its sole negligence. The supreme court responded

> While we do not deny the effect of insurance coverage, we decline to expand the language of our Anti-Indemnity statute to encompass insurance procurement provisions that are not actually indemnity agreements. Rather, we construe the language of the statute strictly to permit parties to contract freely with regard to agreements not covered by the statutory language. Thus the additional insured provision of HB-5357 is not covered by the Anti-Indemnity statute.

Id. 805.

The court referenced the following cases interpreting other types of anti-indemnity statutes wherein additional insured provisions were differentiated from statutorily prohibited indemnity agreements. *See Voisin v. O.D.E.C.O. Drilling Co.*, 744 F.2d 1174, 1177 (5th Cir. 1984), *cert. den'd*, 470 U.S. 1053 (1985)--Longshoremen's and Harbor Workers' Compensation Act § 5(b), 33 U.S.C.A. § 5(b), 33 U.S.C.A. § 905(b) (1976); *Kinney v. G.W. Lisk Co.,* 556 N.E.2d 1090 (1990)--N.Y. Gen. Oblig. Law § 5-322.1 (McKinney 1989) construction and indemnity; *Bosio v. Branigar Organization, Inc.,* 506 N.E.2d 996 (1987)--ILL. REV. CIV. STAT. ch. 29, par.61 (1985) construction; *Cone Bros. Contracting Co. v.*

Ashland-Warren, Inc. 458 So. 2d 851, 855-56 (Fla. Dist. Ct. App. 1984)–FLA. STAT. ch. 725.06 (1977) construction anti-indemnity. The Louisiana Anti-Indemnity statute expressly prohibits additional insured clauses that shift the burden of insurance. LA. REV. STAT. ANN. § 9:2780(G)(West 1986).

C. Waiver of Recovery: Waiver of Subrogation.

1. Definitions.

a. "Subrogation". "*Subrogation*" is an equitable theory that allows a party who has paid damages or other compensation to another person (damaged party) as a result of a third person's act or omission to "step into the shoes" of the damaged party who has been so paid and to pursue the damaged party's remedies against the party who committed the act or omission. "Subrogation" therefore simply means the substitution of one creditor for another. One common example of a subrogation is an insurance company's subrogation suit against a third party who has caused or contributed to bodily injuries or property damages to the insured, the insured's employees or other persons.

In a commercial leasehold, liability for property damages due to fire or other casualty may be contractual or may result from an independent tort because a party negligently causes damages to the other party's property. The victim of the damage becomes the "creditor" and the perpetrator becomes the "debtor." Most landlords and tenants carry property insurance and liability insurance. The property insurance is an indemnity contract against accidental loss of property while the liability insurance is an indemnity contract against liability to third parties for negligent acts.

The property insurance carrier of the party who suffered the loss has an equitable right of subrogation to take over the right of the insured as a creditor in relation to the debtor who negligently caused the loss. The court in *Finger v. Southern Refrigeration Services, Inc.,* 881 S.W.2d 890 (Tex.App.--Houston [1st Dist.] 1994, *writ denied*) rejected the argument that a property insurer did not have a right to bring suit in the name of the named insured, the landlord, to recover in subrogation against a negligent contractor hired by the tenant. The leased premises burned after an employee of the tenant, a Monterrey House restaurant, tried to restart a heater that had been left in a partially-repaired condition by the tenant's contractor. The tenant had paid for a fire insurance policy which named the landlord as the insured. The contractor argued that the landlord had no damages to which the insurer could be subrogated since the insurer had paid to fix the landlord's building!

When a subrogation claim is made against the liable party, they will undoubtedly tender the defense of the claim to their liability insurer who has contracted to indemnify them from claims of liability. However, the lease normally provides that the parties release each other from liability for damage of the type covered by the damaged party's insurance and each party covenants to cause their respective property insurance company to waive their subrogation rights with the result that the parties will be compensated by their casualty insurers without resulting in any subrogation claims by the insurers against the negligent party.

b. "Waiver of Subrogation". "*Waiver of Subrogation*" is the waiver, in advance, of the equitable right of subrogation of the person paying the damages or other compensation to recover against the third party for the monies so paid.

c. "Waiver of Recovery". "*Waiver of Recovery*" is the waiver, in advance, by one party of such party's right to recover against the other party for damages caused by the other party.

2. Claims for Damage or Loss of Property.

a. Landlord and Tenant Relationship. In the landlord-tenant relationship, the tenant is liable to the landlord if the tenant negligently destroys the premises (*e.g.*, negligently caused fire) absent a provision in the lease to the contrary. *Nagorny v. Gray*, 261 S.W.2d 741 (Tex. Civ. App.--Galveston 1953, *no writ*).

(1) Covenant Requiring Party to Insure its Own Property Not Equivalent to Waiver of Recovery or Waiver or Subrogation. Upon payment by the landlord's insurer for the insured property loss, the landlord's insurer is subrogated to the landlord's claim and can sue the tenant to recoup the insurance proceeds. In *Wichita City Lines, Inc. v. Puckett*, 295 S.W.2d 894 (Tex. 1956), the Texas Supreme Court held that where the lease merely provided that the landlord agreed to carry fire and extended coverage insurance on the building, part of which was occupied by the landlord, there was **no duty on the landlord to procure insurance for the benefit of the tenant**, and the insurers were not precluded from obtaining a subrogated cause of action from payment of damages on account of fire caused by tenant's negligence. The court rejected the tenant's contention that the intent of the parties for including a covenant of the landlord to insure its own building (presumably the cost was built into the rent) was to exculpate the tenant for its own negligence.

(2) Covenant Requiring Other Party to Pay for Insurance Equivalent to Waiver of Recovery by Insured Against Insurance Purchaser. In *Publix Theatres Corp. v. Powell*, 71 S.W.2d 237 (Tex. Comm.App. 1934), the lessee agreed in the lease to carry the fire insurance on the leased building, at the lessee's expense, naming the landlord as the insured. The insurer paid, but the landlord still sued the tenant for the loss. The supreme court declared that to permit the lessor to keep the insurance money and also to collect from the lessee would be a double recovery.

Query: **What about insurer's subrogation claim against insurance purchaser?**

In *Interstate Fire Ins. Co. v. First Tape, Inc.*, 817 S.W.2d 142 (Tex. App.--Houston [1st Dist.] 1991, *writ denied*), the court of appeals refused to limit the waiver of subrogation contained in the lease to claims against the current tenant so as to permit the otherwise subrogated insurer to pursue the former tenant after assignment. First Tape, therefore, was able to retain the protection of the waiver of subrogation clause even after the lease was assigned.

(3) Rationale for Waivers of Subrogation. Since the landlord's primary interest is insuring the landlord's improvements, and the tenant's primary interest is in insuring the tenant's property, why make the other party liable for a risk that is already insured? Because both parties can be protected by insurance, neither is particularly interested in imposing liability on the other. The issue is how to allocate the risk of loss--or, more precisely, which party should pay the property insurance premiums.

(a) Avoids Double Coverage. To require each party to carry coverage for negligently causing damage to another party's property forces the landlord and the tenant to insure both the landlord's and the tenant's property, which results in each insuring its own and the other party's property. To avoid this need for double coverage each party can agree to look to its own insurance carrier for property loss caused by the acts or omissions of the other party and waive rights of recovery and subrogation against each other. If both landlord and tenant are to be liable for the risk of negligently caused loss to the property of the other, then the landlord and every tenant in a multi-tenant project must not only be sure to have a policy for its own property but must be sure that their liability insurance is sufficient to cover the replacement cost of the entire building and all of tenants' property therein. A more sensible approach is to have the landlord take out a casualty policy and have the premium costs paid by the tenants in the building under an operating cost pass-through provision in the lease.

(b) Allocates Risk to Property Insurer. A waiver of subrogation clause assures that the insurance carrier for the property owner pays for the property loss as opposed to the other party's (the negligent landlord's or tenant's, as the case may be) liability insurance carrier. *See* Hagan, *Using Waivers and Indemnities in Commercial Leases,* THE PRACTICAL REAL ESTATE LAWYER 11 (1993), also repeated at ALI- ABA'S PRACTICE CHECKLIST MANUAL FOR DRAFTING LEASES: Checklists, Forms, and Drafting Advice from *The Practical Lawyer* and *The Practical Real Estate Lawyer* 149 (1994), for the rationale that the appropriate allocation of risk is to require each party to insure its own property and waive recovery, and waive subrogation against the other for damages to each other's property due to the negligence of either party.

(c) Usually Inadequate Liability Insurance to Cover Risk. Why is this the best approach? This question incorrectly assumes that there is adequate liability insurance to cover the loss. Many times there will be no liability insurance because the party self-insures. The more likely situation is that the liability insurance policy of the negligent party will have limits far short of the loss involved (for example, where a negligent employee of the tenant leaves the coffee pot on at night which results in a large office building burning down). In a large multi-tenant building, the loss could easily exceed the liability insurance coverage of a small tenant. Even if there is sufficient property loss coverage under the liability policy, there usually is a large deductible and dissipation of the time and energy in a contest between the insurance companies and the parties over the issue of who negligently caused the fire.

(d) Risk Already Factored in to Property Insurance Premium. Also, more importantly, is the fact that claims against property insurance are much less likely to result in higher premiums or loss of coverage than claims against the liability insurance. The property insurance carrier has more than likely already calculated its premium based on the assumption that it will not be able to recoup its costs via subrogation against a negligent tenant.

(4) Waivers. Waiver of recovery is the landlord or tenant waiving its rights or recovery for the acts of the other. Waiver of subrogation is the landlord or tenant or both waiving the right of its insurer to be subrogated to the landlord's or tenant's claim. While a waiver of recovery also is a waiver of subrogation (because the insurer has no rights left to which to be subrogated), a waiver of subrogation alone is not a waiver of recovery.

(a) Valid Despite Negligence of Released Party. In Texas, waiver of recovery and waiver of subrogation clauses are valid. *See International Co. v. Medical-Professional Building of Corpus Christi*, 405 S.W.2d 867 (Tex. Civ. App.--Corpus Christi 1966, *writ ref'd n.r.e.*)--lessee waived in advance any claims for damages caused by lessor's negligent failure to maintain boilers in portion of premises under landlord's control "to extent that lessee was compensated by insurance for such damages;" and *Williams v. Advanced Technology Ctr., Inc.*, 537 S.W.2d 531 (Tex. App.--Eastland 1976, *writ ref'd n.r.e.*)--subrogation suit brought against lessee by lessor's fire insurance carrier was barred by lessor's waiver of subrogation clause contained in lease, notwithstanding lessee's breach of the lease by permitting the leased premises to be used for an extra hazardous operation.

(b) Scope of Released Parties. The care with which waiver of recovery and waiver of subrogation clauses should be drafted is illustrated by a recent Louisiana case. *RTC v. Gasper-Virgillio a/k/a "Sonny" Virgillio,* 27 F.3d 178 (5th Cir. 1994). Club Daiquiris burned to the ground as a result of a the negligent use by Sonny Virgillio, an employee of the tenant, of combustible material "to facilitate the removal of the fixtures." Subsequent to the execution of the lease, the tenant assigned the lease to a joint venture of which it was a joint venturer. ISLIC, the insurer of the landlord, sued in subrogation, to collect from Susson, Inc., the tenant named in the lease, for the damages paid by the insurer to the landlord. The lease contained the following waiver provision:

Provision:

> Lessor will keep the leased premises insured against loss or damage by fire, with the usual commercial extended coverage endorsements, and in the event of loss, neither lessor nor its insurer shall have any recourse against lessee, it being understood and agreed that the lessor assumes all risk of damage to its own property arising from any insured risk.

The Fifth Circuit, applying Louisiana law, held that under Louisiana law, the assumption of all risk by the landlord and waiver of recourse against the tenant

relieved the tenant of liability for its own negligence; therefore, the joint venture was not liable for the negligent acts of its employee. But the court found that the waiver provision did not specifically include a waiver of recovery against "employees, agents, servants, or officers" and therefore did not prevent recovery against the employees or officers of the originally-named tenant, or of the successor tenant. The express negligence test is not the law in Louisiana. *Id.* n.1, p. 180. In order for this provision to have the same result in Texas, it would have to expressly provide that the lessor waived (released) all claims against the ...

Provision:

> tenant, its successors and assigns, and the employees, agents, servants, and officers, of the tenant and its successors and assigns, for damage to the landlord's property arising out of the negligence of the tenant, its successors and assigns, and the employees, agents, servants, and officers of tenant, and its successors and assigns.

See Dresser Industries, Inc. v. Page Petroleum, Inc., 853 S.W.2d 505 (Tex. 1993) discussed at **Article IV--Exculpation Provisions and Releases**

(c) Waiver as to Specific Risk or Insurance Proceeds? Should the waiver extend to specified risks or only to the extent of the proceeds actually recovered from the insurer? If the waiver is only as to the insurance proceeds, then the parties are exposed for the deductible or losses in excess of the other party's insurance coverage.

(d) Express Negligence. The waiver should expressly cover loss due to the negligence of the other party. Although no Texas case has yet addressed whether the waiver of subrogation clause must meet the fair notice requirements, such clauses are exculpation clauses identical in effect as those held unenforceable for failing to meet the fair notice requirements, including the express negligence test, in *Dresser Industries, Inc. v. Page Petroleum, Inc.* 853 S.W.2d 505 (Tex. 1993). If so, then **most waiver of subrogation clauses in standard use are not enforceable as written**!

(e) Scope of Risk Covered. Care should be taken in drafting the scope of the waiver of subrogation. A waiver of subrogation as to "the premises" does not include the tenant's furniture, equipment, machinery, goods or supplies which the tenant might bring on to the premises. *See International Medical Sales, Inc. v. Prudential Ins. Co. of America*, 690 S.W.2d 84 (Tex. Civ. App.--Dallas 1985, *no writ*).

(f) Verification of Effect of Waivers on Insurance Coverage and Cost of Insurance Coverage. Before the parties agree to waivers of recovery or subrogation, they should verify that their respective insurance policies will not be voided due to the waiver. Also, the parties should determine, in advance, if the waivers will impact the cost of coverage. Confirmation of endorsement reflecting contractual indemnity, waiver of subrogation and additional insured/loss payee should be verified as a condition of extending the waivers.

(g) Coordination with Other Contractual Provisions. The waiver of subrogation and other provisions of the contract may be inconsistent leaving ambiguities as to the parties' intent. A lease may require the tenant at the termination of the lease to return the leased premises in its original condition except for "reasonable wear and tear and damage by casualty not occurring through the tenant's negligence". Such a clause is potentially in conflict with a waiver of subrogation clause. Similarly, a provision whereby a tenant indemnifies the landlord for loss arising out of the tenant's negligence is in conflict with the waiver of subrogation provision. The indemnity provision in such case needs to exclude the loss covered by the waiver of subrogation provision.

(h) Implied Waivers of Subrogation. Some courts have implied a waiver of subrogation when the contract did not contain an express waiver of subrogation. In *Lumber Mutual Ins. Co. v. Zoltek Corp.,* 647 N.E.2d 395 (Mass. 1995) the Massachusetts supreme court held that the landlord intended a tenant to be a co-insured and the beneficiary of an implied waiver of subrogation against the tenant for its negligently caused damage to the landlord's property, where the leased contained a provision obligating the tenant to maintain the premises in good condition "damage by fire or other casualty excepted", the tenant paid a portion of the landlord's insurance premiums through an operating expense pass through clause, and the landlord had expressly provided that the tenant was not required to carry property insurance on the building.

b. Owner and Contractor Relationship. Waivers of subrogation have been upheld in numerous construction contract cases. *See* Snodgrass, *Waiver of Subrogation and Allocation of Risk in Construction Contracts,* 62 DEF. COUNS. J. 95 (Jan. 1995). *See* **Appendix 1, AIA Document A201-General Conditions of the Contract for Construction, Paragraph 11.3.7 (1997 Ed.)**. Waivers of subrogation in the AIA system are designed to shift to the owner and its property insurance carrier the risk of loss to the project during construction. Such provisions are a valid risk allocation for the following reasons: (1) They avoid disruption and disputes between the parties involved in the construction project; (2) They allow the parties to identify and allocate the risks associated with the project; and (3) They allow one party to contract to provide the property insurance for all risks associated with the project for all parties. Under the AIA documents, the owner is responsible for obtaining the type and amounts of property coverage.

(1) Parties Released. The form of waiver of subrogation contained in the AIA documents is a "waiver of recovery" between the parties (*e.g.,* the owner and the contractor in Paragraph 11.3.7 to the **AIA A201 General Conditions of the Contract for Construction**. **See Appendix 3**), but also is a waiver of recovery by the parties against "any of their subcontractors, sub-subcontractors, agents and employees" and requires that these third parties similarly provide a waiver of recovery against all such parties to the project.

Provision: Par. 11.3.7 AIA Document A201

> The Owner or Contractor, as appropriate, shall require of the Architect, Architect's consultants, separate contractors described in Article 6, if any, and the subcontractors, sub- subcontractors, agents and employees of any of them, by appropriate agreements, written where legally required for validity, similar waivers each in favor of other parties enumerated herein.

However, courts have permitted the insurer to subrogate and sue such other third parties, such as the architect, despite the AIA broad listing of released parties, where the owner required the architect to maintain errors and omissions insurance. *St. Paul Fire & Marine Ins. Co. v. Freeman-White Assoc.s, Inc.,* 366 N.E.2d 480 (N.C. 1988).

(2) Scope of Liabilities Released. The waiver of subrogation contained in the AIA A201 waives recovery between the parties to the extent covered by property insurance applicable to the Work.

Provision:

> for damages caused by fire or other perils **to the extent covered by property insurance** obtained pursuant to Paragraph 11.3 or other property insurance **applicable to the Work**....

Since releases are construed by courts narrowly, the AIA waiver of subrogation language has been interpreted narrowly. In *SSDW Co. v. Brisk Waterproofing Co.,* 556 N.E.2d 1097 (N.Y. 1990), a New York court held that the waiver clause found in the AIA Construction Projects of a Limited Scope form applied only to damages occurring to areas within the limits of the "**work**" and not to the parts of the building outside the "work". *Also see Public Employees Mutual Ins. Co. v. Sellen Constr. Co.,* 740 P.2d 913 (Wash. App. 1987).

The **time period covered** by the "waiver" has been the subject of litigation. In *Automobile Ins. Co. v. United H.R.B.,* 876 S.W.2d 791 (Mo. App. 1994) an insurer of the owner brought a subrogation action against a contractor for property damaged caused by a fire that occurred five months after final payment had been made to the contractor and after the owner had exclusive control of the premises. The court found an ambiguity between the AIA provisions. The contractor took the position that it had an insurable interest in the property as long as the owner maintained the insurance policy in effect at the time the work was being done. The court, however, held that the waiver of subrogation provision no longer applied after final payment because the contractor no longer had an insurable interest in "the work".

(3) Clarifications as to Other Contractual Requirements. The AIA Waiver of Subrogation contains the following provision clarifying that certain other risk allocation provisions do not void the allocation to the insurer of property damage risk.

Provision:

> A waiver of subrogation shall be effective as to a person or entity even though that person or entity would otherwise have a duty of indemnification, contractual or otherwise, did not pay the insurance premium directly or indirectly, and whether or not the person or entity had an insurable interest in the property damaged.

(4) Fair Notice Requirement. The AIA Waiver of Subrogation provision is drafted as a waiver of recovery. However, this provision does **not** meet the fair notice requirements for releases articulated in *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993) in order to release liabilities arising out of the Released Party's negligence. The provision is neither conspicuous nor does it expressly refer to the negligence of the party being released.

Forms of waiver of recovery and subrogation in a lease are contained in **Appendix 7**; and for construction contracts are contained in **Appendix 15)**, AIA Document A201-General Conditions of the Contract for Construction for attachment to AIA Document A101-Standard Form of Agreement Between Owner and Contractor, Paragraph 11.3.7.

3. Bodily Injury. In relationships between two parties with employees subject to workers' compensation insurance, the parties should consider waiving, in advance, the workers' compensation insurance carrier's right by way of subrogation to recoup amounts paid as compensation to the employee for the employee's injuries from the other party for its liability to the injured employee [*e.g.*, landlord requiring the tenant/employer to waive the tenant's claim (*i.e.*, insurer's claim)] for contribution or reimbursement for amounts paid to compensate the injured employee arising in whole or in part out of the negligent act or omission of such party (the landlord). Waiver of subrogation as to workers' compensation carrier's claims has been upheld as valid in Texas. *National Union Fire Ins. Co. of Pittsburgh, Pa. v. Pennzoil Co.*, 866 S.W.2d 248 (Tex. App.--Corpus Christi 1993, *no writ*).

The court in *Hartford Accident & Indemnity Co. v. Buckland*, 882 S.W.2d 440 (Tex. App.–Dallas 1994, *writ denied*) held that the waiver of subrogation contained in the endorsement to the workers' compensation policy issued by Hartford Accident to Fish Engineering and Construction, Inc. waived both Hartford Accident's statutorily-granted right to be reimbursed for payments previously paid to the injured employee and its right to a credit for future benefit payments it still had to pay against the employee's recovery against the negligent third party.

A typical form of waiver of subrogation in a lease is set forth in **Appendix 7**.

4. Insurance Policy Endorsements.

a. Liability Policies. The standard form CGL policy, the ISO commercial general liability form CG 00 01, is silent as to pre-loss waivers, although it expressly prohibits post-loss waivers. ISO has promulgated the following endorsement forms for use with its standard types of liability policies:

(1) CGL. **CG 24 04 10 93 "Waiver of Transfer of Rights of Recovery Against Others to Us"** endorsement. **Appendix 23**.

The TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHERS TO US Condition (Section IV - COMMERCIAL GENERAL LIABILITY CONDITIONS) is amended by the addition of the following:

We waive any right of recovery we may have against the person or organization shown in the Schedule above because of payments we make for injury or damage arising out of your ongoing operations or "your work" done under a contract with that person or organization and included in the "products-completed operations hazard." This waiver applies only to the person or organization shown in the Schedule above.

(2) Owners and Contractors Protective. **CG 29 88 10 93** endorsement. **Appendix 24.**

The TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHERS TO US Condition (Section IV) is amended by the addition of the following:

We waive any rights of recovery we may have against the person or organization shown in the Schedule above because of payments we make for "bodily injury" or "property damage" arising out of your ongoing operations. This waiver applies only to the person or organization shown in the Schedule above.

(3) Commercial Auto. **CA 00 01**.

5. TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHER TO US

   If any person or organization to or for whom we make payment under this Coverage Form has rights to recover damages from another, those rights are transferred to us. That person organization must do everything necessary to secure our rights and must do nothing after "accident" or "loss" to impair them.

b. Property Policies. Many commercial property policies and inland marine policies include subrogation clauses that imply permission to grant pre-loss waiver. However, some forms may specifically deny the insured the right to waive subrogation. The ISO form expressly recognizes the right of the insured to waive subrogation. The following is the subrogation clause contained in the **ISO Commercial Property Conditions Form CP 00 90**:

TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHERS TO US

If any person or organization to or from whom we make payments under this Coverage Part has rights to recover damages from another, those rights are transferred to us to the extent of our payment. That person or organization must do everything necessary to secure our rights against another party in writing:

1. Prior to a loss to your Covered Property or Covered Income.

2. After a loss to your Covered Property or Covered Income only if, at time of loss, that party is one of the following:

   a. Someone insured by this insurance;

   b. A business firm:

      (1) Owned or controlled by you; or

      (2) That owns or controls you; or

   c. Your tenant.

This will not restrict your insurance.

Builders risk insurance is written on a variety of forms. Therefore, it is important to determine whether the policy prohibits waiver of subrogation. The typical mutual waiver of subrogation in the owner-contractor construction contract form may invalidate the builder's risk coverage.

The following is the **ISO Builders Risk Coverage Form CP 00 20 10 91** provision:

4. Waiver of Recovery Against Others

   You may not waive your rights to recover damages from an architect, engineer or building trades contractor or subcontractor with respect to the described premises except as agreed to in writing by us. This provision supersedes any provision to the contrary in the TRANSFER OF RIGHTS OF RECOVERY AGAINST OTHERS TO US Commercial Property Conditions.

D. Certificates of Insurance. As a general rule, certificates of insurance do not govern the insurance policy's coverage. A certificate of insurance can be misleading in several ways and provide a false sense of security that the policy matches the certificate. Hamilton, *Problems Arising From Additional Insureds Endorsements-Dealing With An Additional Insured Certificate Is Not As Simple As It May Seem, For There Are Many Pitfalls to Be Faced*, 62 DEF. COUNS. J. 384 (July 1995).

Being designated as a Certificate Holder does not make the certificate holder an insured, additional insured, or a third party beneficiary covered by the policies insurance. *Gracida v. Tagle*, 946 S.W.2d 504 (Tex.App.-- Corpus Christi 1997, *no writ*).

1. ACORD. **Appendixes 8 and 9** contain a copy of the ACORD form of Certificate of Insurance 25-S. The **ACORD 25-S** certificate contains the following qualifications:

Provision: Certificate does not create coverage.

This certificate does **not** amend, extend or alter coverage afforded by the policies below.

Provision: Certificate does not state prior claims on limits.

Preservation of Policy Provisions
This is to certify that the policies of insurance listed below have been issued to the insured named above for the policy period indicated. Notwithstanding any requirement, term or condition of any contract or other document with respect to which this certificate may be issued or may pertain, the insurance afforded by the policies described herein is **subject to** all of the terms, exclusions and conditions of such policies. Limits as shown may have been reduced by paid claims.

Provision: No duty to notify certificate holder.

Cancellation
Should any of the above described policies be cancelled before the expiration date thereof, the issuing company will **endeavor** to mail ___ day's written notice to the certificate holder named to the left **but failure** to mail such notice shall impose no obligation of liability of any kind upon the company, its agents or representatives.

The certificate holder should require the following modifications to the ACORD 25-S:

(1) The certificate of insurance should be amended to require prior notification of cancellation or material change to the policy's coverage.

(2) The certificate of insurance should be amended to state the extent of prior claims against the insured limits or to provide for a separate limit applicable to the additional insured's project.

(3) The certificate of insurance should be amended to acknowledge that the policy premium has been paid for the indicated insurance, including for the endorsement to add the additional insured to the policy.

(4) The certificate of insurance should be amended to provide that the additional insured is insured for its concurrent and sole negligence. The contract with the Indemnifying Party should also contain these same representations and covenants.

(5) The certificate of insurance should be amended to provide that in the event of conflict between the certificate and the policy the certificate controls and amends the policy.

In *J.M. Corbett Co. v. Insurance Co. of North America*, 357 N.E.2d (Ill. App. 1984) the court held that the indemnity language typed on the certificate created a separate contract between the insurer and the additional insured providing broader coverage than what was afforded by the policy.

2. Policy Controls. Common problems with certificates of insurance include the possibility that certificates issued by agents contain errors and the possibility that the certificates fail to reveal special limitations applicable to the coverage afforded. Some courts take the position, based on language similar to the above-quoted language from the ACORD 25-S Form, that a certificate of insurance does not create coverage. See *S.L.A. Property Management v. Angelina Casualty Co.*, 856 F.2d 69 (8th Cir. 1988) (certificate listing a different person as the additional insured did not control over actual listing on policy endorsement); and *Mercado v. Mitchell*, 264 N.W.2d 532 (Wis. 1978).

IV. Exculpation and Limitation of Liability Provisions and Releases.

A. Distinguished from Indemnity Provision. *See* Ikard, *Exculpatory Clauses and Their Effectiveness to Protect Drafters and Fiduciaries*, 18th ADVANCED ESTATE PLANNING AND PROBATE COURSE (STATE BAR OF TEXAS 1994); Annot., 49 A.L.R.3d 321, *Validity of Exculpatory Clause in Lease Exempting Lessor from Liability* (1973); Annot., 30 A.L.R.4th 971, *Applicability of Exculpatory Clause in Lease to Lessee's Damages Resulting From Defective Original Design or Construction* (1984); Annot., 8 A.L.R. 1393, *Validity, Construction and Effect of Agreement Exempting Operator of Amusement Facility from Liability for a Personal Injury or Death of Patron* (1966); Annot., 66 A.L.R. 4th 622, *Liability for Injury Incurred in Operation of Power Golf Cart* (1988); Annot., 88 A.L.R.3rd 1236 *Liability of Youth Camp, its Agents or Employees, or of Scouting Leader or Organization for Injury to Child Participant in Program* (1978); Annot., 73 A.L.R.4th 496, *Liability of Local Government Entity for Injury Resulting from Use of Outdoor Playground Equipment at Municipally Owned Park or Recreational Area* (1989). Springer, *Releases: An Added Measure of Protection from Liability*, 39 BAYLOR L.REV. 487 (1987); Smith, *Selected Topics in Lease Drafting: Indemnities, Waivers, Disclaimers and Remedies*, ADVANCED REAL ESTATE DRAFTING COURSE Q (STATE BAR OF TEXAS 1990).

1. Definitions.

a. "Exculpation". Example: "I am not liable ... ." An "*exculpatory*" provision is defined as a provision that "clears or tends to clear a person from alleged fault or guilt; excusing." BLACK'S LAW DICTIONARY, p. 566 (6th Ed., 1990). An exculpatory provision is designed to exclude, as between the parties to a contract, certain designated duties, liabilities or costs due to the occurrence or non-occurrence of events.

b. "Releases". Example: "You are not liable ...." A "*release*" is defined as

> A contractual arrangement whereby one party assumes the liability inherent in a particular situation, thereby relieving the other party of responsibility ... . [An] [a]greement or contract in which one party agrees to hold the other without responsibility for damage or other liability arising out of the transaction involved.

BLACK'S LAW DICTIONARY, p. 658 (5th Ed., 1979).

c. "Limitation of Liability". Example: "If I am liable, my liability to you is limited to $___." A "*limitation of liability*" provision sets an upper limit to the amount recoverable by one party against the other.

2. Characteristics.

a. Rights or Obligations between Parties.

(1) Indemnity. An indemnity rather than extinguishing a cause of action, creates a potential cause of action in the Indemnified Person against the Indemnifying Person. If the undertaking is to indemnify against liability, the cause of action matures when the Indemnified Person incurs liability covered by the agreement. But, if the obligation is to indemnify against the loss incurred by the Indemnified Person, the cause of action matures when the loss has been realized. *See Wallerstein v. Spirt,* 8 S.W.3d 774 (Tex.App-Austin [3rd Dist.] 1999, *no writ*)-involving an indemnity by partners but not a release between partners.

(2) Release. A release surrenders legal rights or obligations between the parties to the agreement. *Cox v. Robinson*, 150 S.W. 1149, 1155 (Tex. 1912); *Quebec v. Gulf, C. & S. F. R. Co.*, 81 S.W. 20, 21-22 (Tex. 1904). A release extinguishes the claim or cause of action as effectively as would a prior judgment between the parties and is an absolute bar to any right of action on the released matter. *Hart v. Traders & General Ins. Co*., 189 S.W.2d 493, 494 (Tex. 1945). For these reasons, a release is expressly designated as an affirmative defense. TEX. R. CIV. P. 94.

(3) Limitation of Liability. Limitation of liability provisions are not subject to a penalty analysis because, by their nature, they cannot be used to penalize a party for a breach of contract. *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*) and *Fox Elec. Co. v. Tone Guard Sec. Inc.,* 861 S.W.2d 79, 83 (Tex.App.-Ft. Worth 1993, *no writ*).

A limitation of liability provision is not a liquidated damage provision. A liquidated damage provision fixes liability at a specific amount or at a specified percentage of the consideration paid under a contract. Unlike a limitation of liability provision, a liquidated damage provision must satisfy the following penalty analysis: (1) the harm caused by the breach must be incapable of being estimated or be difficult to estimate at the time of entry into the agreement, and (2) the amount of liquidated damages called for must be a reasonable forecast of just compensation. *See Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*) [limitation of liability provision contrasted to liquidated damage provision]; *Vallance & Co. v. D'Anda*, 595 S.W.2d 587, 589 (Tex.Civ.App.-San Antonio 1980, *no writ*); and *Phillips v. Phillips,* 820 S.W.2d 785 (Tex. 1991).

b. Liabilities to Third Parties.

(1) Release. A release extinguishes any actual or potential claim for liability and injury the "releasor" (the "***Releasing Party***") might have against the "releasee" (the "***Released Party***"), without regard to the Released Party's actual or potential liability to third parties. *See Whitson v. Goodbodys, Inc.*, 773 S.W.2d 381, 383 (Tex. App.--Dallas 1989, *writ denied*).

(2) Indemnity. An indemnity does not relate to liability claims between the parties to the agreement, but obligates the Indemnifying Person to protect the Indemnified Person against liability claims of persons not a party to the agreement.

The following is an example of an exculpatory provision in a commercial lease:

Provision:

> **Section 2: WAIVER - No Indemnified Person shall be liable in any manner to Tenant or any other party for any injury to or death of persons or for any loss of or damage to the property of Tenant, its employees, agents, customers, invitees, or of others, regardless of whether such property is entrusted to employees of the Building, or such loss or damage is occasioned by casualty, theft, or any other cause of whatsoever nature, whether or not due in whole or in part to the negligence or strict liability of the Indemnified Person, unless caused by the willful misconduct or gross negligence of an Indemnified Person. In no event shall any Indemnified Person be liable in any manner to Tenant or any other party as the result of the acts or omissions of Tenant, its agents, employees, contractors or any other tenant of the Building. All personal property upon the Leased Premises shall be at the risk of Tenant only, and none of the Indemnified Persons shall be liable for any damage thereto or theft thereof, whether or not due in whole or in part to the negligence of any Indemnified Person.**

B. Elements.

1. Requirement to Be Conspicuous.

In *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993), the following provisions contained in work orders of Dresser and Houston Fishing Tools Company were examined by the Texas Supreme Court:

Dresser Provision:

> There are obviously many conditions in and about the well of which we can have no knowledge and over which we can have no control. Therefore, we (Dresser) accept this service order only on condition that we do not guarantee any particular result from services to be performed hereunder. Except where damage or injury caused by gross or willful negligence on our part, (Page) shall indemnify (Dresser) and hold (Dresser) free and harmless from all claims for personal injuries, including death and damage, including subsurface damage or injury to the well and damages attributable to pollution or contamination and cost of control and removal thereof, alleged to have been caused by our operations under this service order, including claims alleging that injuries or damages were caused by (Dresser's) negligence, whether such claims are made by (Page), were caused by (Dresser's) negligence, whether such claims are made by (Page), by (Page's) employees, or by third parties. (Emphasis added by author.)

Houston Fishing Tools Provision:

> (A) (Houston Fishing Tools) shall not be liable to (Page) on any theory of legal liability against which (Houston Fishing Tools) may legally contract for any injury or damage to persons ... or to property (whether subsurface or not, including reservoir loss) and any losses arising out of such damage where such damage is sustained in connection with, arising out of, or resulting from the service or material used in the service.
>
> (D) The theories of liability referred to in (paragraph (A) ... include, but are not limited to, breach of express or implied warranty and the sole or concurrent negligence of (Houston Fishing Tools). (Emphasis added by author.)

Page Petroleum drilled a well located in Colorado County to a depth of 11,000 feet and contracted with Dresser to conduct log tests. Houston Fishing Tools was called in to "fish" out Dresser's equipment that became stuck in the well bore. While Houston Fishing Tools was attempting to dislodge the equipment, it lost several thousand feet of wireline and drill pipe down the hole which could not be retrieved. Page attempted to clear the hole by performing a side procedure. This side procedure was not successful; therefore, Page plugged and abandoned the well and was forced to drill a new well. Page then brought suit against Dresser and Houston Fishing Tools alleging negligence and seeking compensation for damages to the original well. Both Dresser and Houston Fishing Tools defended the suit based on the contractual provisions recited above.

The jury attributed liability 50% to Page, 40% to Houston Fishing Tools and 10% to Dresser.

The court of appeals construed the Dresser provision as an "indemnity" and therefore could not exculpate Dresser from its own negligence. Since the Dresser provision was an indemnity, the court held that reference to Page indemnifying Dresser from claims by Page (*see* underlined language in Dresser provision) was clearly inadvertent and repugnant to the intent of the parties. Once the court of appeals determined the clause to be an indemnity, it found that as an indemnity it could not be an exculpation or release operating to extinguish a claim between the parties to a suit.

Conversely, the court of appeals found that the Houston Fishing Tools provision was a "release" which exculpated Houston Fishing Tools from liability to Page.

The supreme court held that compliance with the fair notice requirements is a question of law for the court, overruling *Goodyear Tire & Rubber Co. v. Jefferson Const. Co.*, 565 S.W.2d 916 (Tex. 1978). The supreme court then found that the Dresser and the Houston Fishing Tools provisions were both **not conspicuous as a matter of law**.

a. Indemnity, Releases, Exculpations: Effect the Same. Following the reasoning of the dissent in the court of appeals' decision, the supreme court found that, whether the provision was couched as an indemnity, a release or an exculpation provision, the effect was the same, to transfer the risk of liability for

one's own negligence. The court stated its reasoning as follows:

> As Justice Vance stated in his dissenting opinion in the court of appeals, these agreements, whether labeled as indemnity agreements, releases, exculpatory agreements, or waivers, all operate to transfer risk. ... Although we recognized that most contractual provisions operate to transfer risk, these particular agreements are used to exculpate a party from the consequence of its own negligence. Because indemnification of a party for its own negligence is an extraordinary shifting of risk, this Court has developed fair notice requirements which apply to these types of agreements. The fair notice requirements include the express negligence doctrine and the conspicuous requirement. *Enserch Corp. v. Parker*, 794 S.W.2d 2, 8 (Tex. 1990). ... the conspicuous requirement mandates "that something must appear on the face of the [contract] to attract the attention of a reasonable person when he looks at it." *Ling & Co. v. Trinity Sav. & Loan Ass'n*, 482 S.W.2d 841, 843 (Tex. 1972).
> ...
> [w]e can discern no reason to fail to afford the fair notice protections to a party entering into a release when the protections have been held to apply to indemnity agreements and both have the same effect. ... This is especially true because of the difficulty often inherent in distinguishing between these two similar provisions.

Id. 508.

The same rules have been held to apply to *limitation of liability* provisions. *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*). The court of appeals in *Arthur's Garage* upheld the following limitation of liability provision, limiting an alarm company's liability to $350 in connection with damages sustained by Arthur's Garage when a smoke detector failed to operate:

Provision:

> Liquidated Damages and Indemnification. It is expressly understood and agreed that seller is not an insurer and that insurance, if any, covering personal injury and property loss or damage on purchaser's premises shall be obtained by the purchaser; that the payments provided for herein are based solely on the value of the system and/or service as set forth herein, and are unrelated to the value of the purchaser's property or the property of others located on purchaser's premises; that seller makes no guarantee or warranty including any implied warranty of merchantability or fitness that the system or service supplied will avert or prevent occurrences or the consequences therefrom which the system or service is intended to detect or avert.
>
> Purchaser acknowledges that it is impractical and extremely difficult to fix the actual damages, if any, which may proximately result from a failure to perform any of the obligations herein or a failure of the service and/or system to operate because of, among other things: the uncertain amount or value of purchaser's property or the property of others which may be lost or damaged; the uncertainty of the response time of the police or fire department or other appropriate agency; the inability to ascertain what portion, if any, of any loss would be proximately caused by seller's failure to perform any of its obligations or failure of its equipment to operate; the nature of the services to be performed by seller.
>
> If there shall, notwithstanding the above provisions, at any time be or arise any liability on the part of seller by virtue of this agreement or due to the negligence of seller or otherwise, such liability is and shall be limited to the sum of three hundred fifty and no/100 dollars ($350.00), which sum shall be paid and received as liquidated damages, such liability as herein set forth is fixed as liquidated damages and not a penalty and this liability shall be complete and exclusive.
>
> In the event purchaser desires seller to assume greater liability for the performance of its services hereunder, a choice is hereby given of obtaining full or limited liability by paying an additional amount, proportioned to the responsibility, and an additional rider shall be attached to this agreement setting forth the additional liability of the seller and additional charge.
>
> The rider and additional obligation shall in no way be interpreted to hold seller as an insurer. (emphasis added)

The court found that this provision was **not** a liquidated damage provision, but rather was a limitation of liability provision. As such the provision was not subject to penalty analysis. The provision set a limit to the liability of alarm company to its customer. The alarm contract also included an indemnity. The indemnity was also upheld and is discussed above. The court found the limitation of liability provision and the indemnity were conspicuous (all caps) and expressly covered the negligence of the alarm company.

But see Reuben H. Donnelley Corp. v. McKinnon, 688 S.W.2d 612 (Tex.App.-Corpus Christi 1985, *writ ref'd n.r.e.*) finding that limitation of liability clauses do not limit liability for **tort** liabilities (but the *Donnelley* decision and the cases cited by it may turn on the court's finding that the telephone company occupies a monopolistic position and a conclusion that it is against public policy to enforce limitation of liability provisions in contracts with a public service utility) and *DeKalb Hybrid Seed Co. v. Agee,* 293 S.W.2d 64 (Tex.Civ.App.-Beaumont 1956, *writ ref'd n.r.e.*)(an order form for baby chicks contained a clause limiting the seller's liability to the price of the chicks, court held clause did not apply to seller's **fraud**, an intentional tort); *as contrasted* to *Wade v. Southwestern Bell Tel. Co.,* 352 S.W.2d 460 (Tex.Civ.App.-Austin 1961, *no writ*), *Southwestern Bell Tel. Co. v. Delanney,* 809 S.W.2d 493 (Tex. 1991, Gonzalez, J., concurring op.)(contract limited liability: "The applicant agrees that the telephone company shall not be liable for errors in or omissions of the directory advertising beyond the amount paid for the directory advertising omitted in which error occurs for the issue life of the directory involved."), *Vallance & Co. v. DeAnda*, 595 S.W.2d 587 (Tex.Civ.App.-San Antonio 1980, *no writ*)("...such liability is and shall be limited to a sum equal in amount

to the service charge hereunder for a period of service not to exceed six months...."[$147 on a $9,500 loss]), and the majority line of cases cited in *Helms v. Southwestern Bell Tel. Co.,* 794 F.2d 188 (5th Cir. 1986); and 5 S. WILLISTON, CONTRACTS § 781A (3d ed. 1961); RESTATEMENT OF CONTRACTS § 339, Comment g (1932); *see* Annot., *Liability of Telephone Company for Mistakes in or Omissions From its Directory,* 47 A.L.R. 4th 882 (1986).

The majority opinion and Justice Gonzalez' concurring opinion in *Southwestern Bell Tel. Co. v. Delanney* did not address whether a properly drafted limitation of liability provision can limit liability for tort liabilities arising out of a contractual relationship. The court in *Southwestern Bell Tel. Co. v. Delanney* found that the liability in question was a contractual liability limited by the limitation of liability provision and was not a liability arising out of a tort. Both a contract breach and a tort breach of duty can arise from the same set of facts. The court in *Southwestern Bell Tel. Co. v. Delanney* addressed such duality as follows:

> The majority below relied on *Montgomery Ward & Co. v. Scharrenbeck,* 146 Tex. 153, 157, 204 S.W.2d 508, 510 (1947), where we quoted from 38 AM.JUR. *Negligence* § 10 (1941) as follows:
>
> > Accompanying every contract is a common-law duty to perform with care, skill, reasonable expedience and faithfulness the thing agreed to be done, and a negligent failure to observe any of these conditions is a tort, as well as a breach of the contract.
>
> In *Scharrenbeck,* the defendant agreed to repair a water heater in plaintiff's home. A short time after repair, the heater ignited te roof, destroying the house and its contents. Although the contract obligated the defendant to put the water heater back in good working order, the law also implied a duty to the defendant to act with reasonable skill and diligence in making the repairs so as not to injure a person or property by his performance. In failing to repair the water heater properly, the defendant breached its contract. In burning down plaintiff's home, the defendant breached a common-law duty as well, thereby providing a basis for plaintiff's recovery in tort....
>
> > *See* PROSSER AND KEETON at 656; 1 J. EDGAR, JR. & J. SALES, TEXAS TORTS AND REMEDIES § 1.03 [4][b] at 1-36 (1990). We applied this analysis in *Jim Walter Homes, Inc. v. Reed,* 711 S.W.2d 617, 618 (Tex. 1986), where we wrote:
> >
> > > The acts of a party may breach duties in tort or contract alone or simultaneously in both. The nature of the injury most often determines which duty or duties are breached. When the injury is only the economic loss to the subject of a contract itself the action sounds in contract alone.

The Fort Worth Court of Appeals in *Fox Elec. Co. v. Tone Guard Sec.,* 861 S.W.2d 79 (Tex.App.-Ft. worth 1993, *no writ*) upheld the following provision resulting in limiting Tone Guard's liability to $250 on a $500,000 fire loss:

Provision:

> **(21) APS IS NOT AN INSURER; LIQUIDATED DAMAGES; LIMITATION OF LIABILITY:** It is understood and agreed: That APS is not an insurer; that insurance, if any, shall be obtained by Subscriber, that the payments provided for herein are based solely on the value of the services as set forth herein and are unrelated to the value of the Subscriber's property, or the property of others located on Subscriber's premises; that APS makes no guaranty or warranty, including any implied warranty of merchantability or fitness that the equipment or services supplied will avert or prevent occurrences [sic] or the consequences therefrom which the system is designed to detect or avert. Subscriber acknowledges that it is impractical and extremely difficult to fix the actual damages, if any, which may proximately result from a failure to perform any of the obligations herein, including, but not limited to installation, service, maintenance or monitoring or the failure of the system to properly operate with resulting loss to Subscriber because of, among other things: (a) The uncertain amount of value of Subscriber's property or the property of others kept on the premises which may be lost, stolen, destroyed, damaged or otherwise affected by occurrences which the system or service is designed to detect or avert; (b) The uncertainty of the response time of any police or fire department, should the police or fire department be dispatched as a result of a signal being received or an audible device sounding; (c) The inability to ascertain what portion, if any, of any loss would be proximately caused by APS's failure to perform or by its equipment to operate; (d) The nature of the service to be performed by APS. Subscriber understands and agrees that if APS should be found liable for loss or damage due to a failure of the installation, maintenance, monitoring, service or equipment in any respect whatsoever, APS's liability shall be limited to a sum equal to the total of six (6) monthly payments or Two Hundred Fifty ($250.00) Dollars, whichever is the lesser, as liquidated damages and not as a penalty and this liability shall be exclusive; that APS shall not be liable for consequential or incidental damages except to the extent of the liquidated damages herein provided; and that the provisions of this Section shall apply if loss or damage, irrespective of cause or origin, results directly or indirectly to persons or property, from performance or nonperformance of the obligations imposed by this contract, or from negligence, active or otherwise, of APS, its agents, servants, assigns or employees. If Subscriber wishes APS to assume a limited liability in lieu of the liquidated damages as hereinabove set forth, Subscriber may obtain from APS a limitation of liability by paying an additional monthly service charge to APS. If Subscriber elects to exercise this option, a rider shall be attached to this Agreement setting forth

> the terms, conditions and amount of the limited liability and the additional monthly charge. Such rider and additional obligation shall in no way be interpreted to hold APS as an insurer.

The court distinguished *Alpha Mktg., Inc. v. Honeywell, Inc.,* 690 S.W.2d 35, 37 (Tex.App.-Dallas 1985, *writ ref'd n.r.e.*) ("damages which may arise due to the faulty operation of the system or failure of services provided")and *McCane-Sondock Protection Sys. v. Emmittee,* 540 S.W.2d 764, 766 (Tex.Civ.App.-Eastland 1976, *no writ*) ("loss to the second party resulting by reason of failure of the performance of the alarm system to operate") on the basis that the courts in these cases held the limitation of liability clauses were not enforceable because there could be no "failure of operation" or "faulty performance" unless the alarm systems were installed and operating properly.

Query: Is a limitation of liability provision limiting liability for tort damages to a specified amount enforceable? If a release in advance for one's liability for negligence is enforceable, why would not a limitation of liability in advance not be enforceable?

b. Adoption of UCC Standard. The supreme court in *Dresser Industries, Inc. v. Page Petroleum, Inc.* adopted the "conspicuous" standard set forth in § 1.201(10) of the Texas UCC applicable to contracts for the sale of goods in this case dealing with the sale of services. The court held that the UCC standard would be applicable both to indemnity and releases that relieve a party, in advance, of responsibility for its own negligence. Section 1.201(10) provides

> A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it. A printed heading in capitals (as: NON-NEGOTIABLE BILL OF LADING) is conspicuous. Language in the body of a form is "conspicuous" if it is in larger or other contrasting type or color. But in a telegram any stated term is "conspicuous."

TEX. BUS. COMM. CODE ANN. § 1.201(10) (Vernon 1994).

In both the Dresser and the Houston Fishing Tool contracts, the provisions are located on the back of a work order in a series of numbered paragraphs without headings or contrasting type. Furthermore, the contracts were found to be not so short that every term in the contracts must be considered conspicuous.

How "conspicuous" is conspicuous? *See* Greer and Collier, *The Conspicuous Requirement: Litigating and Drafting Contractual Indemnity Provisions in Texas After Dresser Industries, Inc. v. Page Petroleum, Inc.*, 35 SO. TEX. L. REV. 243 (1994).

The supreme court in *Littlefield v. Schaefer,* 955 S.W.2d 272 (Tex. 1997), found that a release was **not** conspicuous when it was set in a type font too small to read even though the heading was in larger font (heading was in 4 point font 4 point font and the terms of the release were in smaller font);the release was outlined in a box; the heading was all caps, in bold type and read **"RELEASE AND WAIVER OF LIABILITY AND INDEMNITY AGREEMENT"**; and above the signature line appeared the caption in all caps, bold-faced centered and underlined type the following statement "**I UNDERSTAND MOTORCYCLE RACING IS DANGEROUS. YES, I HAVE READ THIS RELEASE.**" The court did not accept the argument that the release was conspicuous because of its small contrasting type. "Where a party is not able to know what the contract terms are because they are unreadable, as a matter of law the exculpatory clause will not be enforced."

In *In Re H. E. Butt Grocery Co.*, 17 S.W.3d 360 (Tex.App.-Houston [14th Dist.] 2000, *orig. proceeding*) the court of appeals determined that testimony from the injured employee to the effect that he was told not to read a waiver and release was inadmissible parole evidence. The court found that the following notice was unambiguous and supported the conclusion that the employee was aware of the agreement to arbitrate claims and releasing his common law right to sue H.E.B. as a non-subscriber to the state's workers compensation system. The court noted that the notice was in all caps and underlined.

Provision:

> ELECTION OF COMPREHENSIVE BENEFITS, RELEASE, WAIVER, INDEMNITY AND ARBITRATION AGREEMENT
>
> NOTICE: BY SIGNING THIS AGREEMENT, YOU AGREE TO RELEASE AND WAIVE CERTAIN RIGHTS TO SUE YOUR EMPLOYER, THE TRUST, THE TRUSTEE OF THE H. E. BUTT GROCERY COMPANY WELFARE BENEFIT TRUST, THE PLAN, AND THE PLAN ADMINISTRATOR IN EXCHANGE FOR THE AGREEMENT TO PROVIDE CERTAIN BENEFITS THROUGH THE TRUST. YOU AGREE TO INDEMNIFY YOUR EMPLOYER AND THE RELEASED PARTIES IN CERTAIN CIRCUMSTANCES AND YOU AGREE TO ARBITRATE ALL FUTURE DISPUTES. THIS AGREEMENT AFFECTS YOUR LEGAL RIGHTS! READ THIS AGREEMENT CAREFULLY AND MAKE SURE YOU UNDERSTAND IT BEFORE SIGNING IT!

To similar effect is the holding in *Lawrence v. CDB Serv.*, 1 S.W.3d 903 (Tex.App.-Amarillo [7th Dist.] 1999, *aff'd*) as to a waiver of the common law right to sue and election to participate in an employers that was in **bold** type in a 2 page election form.

See discussion of the Conspicuousness requirement in **Article IID1c--Elements of an Indemnity Provision** earlier in this Article.

c. Actual Notice. The court noted that the fair notice requirements are not applicable when the Indemnified Person (Released Person) establishes that the Indemnifying Person (Releasing Person) possesses actual notice or knowledge of the indemnity agreement,

citing generally Cate v. Dover Corp., 790 S.W.2d 559, 561 (Tex. 1990). *Dresser* at 508.

2. Express Negligence Requirement. For the same policy reasons that the supreme court in *Dresser* extended the conspicuous requirement to releases, it held that the companion express negligence doctrine also was to be applied to releases.

> ... we hold that the fair notice requirements of conspicuousness and the express negligence doctrine apply to both indemnity agreements and to releases in the circumstances before us; thus, we disapprove of the *Whitson* opinion. [referring to *Whitson v. Goodbodys, Inc.*, 773 S.W.2d 381, 383 (Tex. App.--Dallas 1989, *writ denied*)].

Dresser Industries, Inc. v. Page Petroleum, Inc., 853 S.W.2d 505, 509 (Tex. 1993); *Doe v. Smithkline Beecham Corp.,* 855 S.W.2d 248 (Tex. App.--Austin 1993, *writ granted*).

The court of appeals in *Rickey v. Houston Health Club, Inc.,* 863 S.W.2d 148 (Tex. App.--Texarkana 1993, *writ granted*)--jogger alleged that indoor astroturf track not suitable as jogging track-- found the following release **failed** the express negligence test:

Provision:

> You agree that you are aware that you are engaging in physical exercise and the use of exercise equipment and club facilities which could cause injury to you. You are voluntarily participating in these activities and assume all risk of injury to you that might result. You hereby agree to waive any claims or rights you might otherwise have to sue the health club, its employees or agents for injury to you on account of these activities. You have carefully read this waiver and release and fully understand it is a release of liability. You further agree to release seller from any liability for loss or theft of personal property.

The court in *Polley v. Odom,* 957 S.W.2d 932 (Tex.App.-Waco 1997, *judgm't vacated*) held that the following "**risk of loss**" provision did not pass the express negligence test as it impliedly but did not expressly release the landlord from liability for its negligence.

Provision:

> Risk of Loss. Except where due to the willful neglect of Lessor all risk of loss to personal property or loss to business resulting from any cause whatsoever shall be born exclusively by Lessee.

3. Prerequisites for Validity. The following prerequisites must be satisfied for a release to be valid:

a. Public Policies.

(1) Oilfield Anti-Indemnity Statute. After refusing to enforce the releases reviewed in the *Dresser* case on the grounds of not being conspicuous, the Texas Supreme Court in footnote 5 notes

> "Although we do note that today's holding would suggest that Chapter 127 (the Texas Oilfield Anti-Indemnity Statute) would apply to releases as well as to indemnity agreements, we do not reach the merits of such an argument."

Dresser at 510.

(2) Equal Bargaining Power. The release must not be the product of "unequal bargaining power" in circumstances involving indispensable services. This test is not well developed. In *Crowell v. Housing Authority of the City of Dallas*, 495 S.W.2d 887, 888-89 (Tex. 1973), the court refused to enforce a landlord-imposed release by the residential tenant of any damages "due to the conditions of these or other premises of the Landlord, from theft or from any cause whatsoever." The court stated

> [T]he situation of (landlord) and its tenants presents a classic example of unequal bargaining power. The terms of the contract are dictated by (landlord), and a prospective tenant has no choice but to accept them if he and his family are to enjoy decent housing accommodations not otherwise available to them.

Id. at 889.

The Texas Supreme Court has defined this condition as being a case where "one party has no real choice in accepting an agreement limiting the liability of the other party." *Allright, Inc. v. Elledge*, 515 S.W.2d 266 (Tex. 1974).

There appears a pattern of cases upholding exculpation provisions in commercial contexts but not in consumer matters. Ellis and Kessler, *Exculpation and Indemnity Clauses*, 23rd ANNUAL MORTGAGE LENDING INSTITUTE 6-7 (UNIV. TEX. 1989) citing on commercial leases: *Barragan v. Munoz*, 525 S.W.2d 559 (Tex. Civ. App.--El Paso 1975, *no writ*); *Mitterlehner v. Mercantile National Bank at Dallas*, 378 S.W.2d 137 (Tex. Civ. App.--Dallas 1964, *writ ref'd n.r.e.*), *Fidelity Union Life Ins. Co. v. Fine*, 120 S.W.2d 138 (Tex. Civ. App.--Waco 1938, *writ dism'd*); and citing on residential leases: *Crowell v. Housing Authority of the City of Dallas*, 495 S.W.2d 887 (Tex. 1973), *Jones v. Houston Aristocrat Apartments, Ltd.*, 572 S.W.2d 1 (Tex. Civ. App.-- Houston [1st Dist.] 1971, *writ ref'd n.r.e.*), and *Taylor v. Gilbert Gertner Enterprises*, 466 S.W.2d 337 (Tex. Civ. App.--Houston [1st Dist.] 1971, *writ ref'd n.r.e.*). *Also see Corpus Christi National Bank v. Gerdes*, 551 S.W.2d 521 (Tex. Civ. App.--Corpus Christi 1971, *writ ref'd n.r.e.*) in which the court upheld a release clause in a will releasing, in advance, gross negligence of a Testamentary Trustee.

The court of appeals in *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*) upheld the limitation of liability provision (set out above), which limited an alarm company's liability to $350 in connection with damages sustained by Arthur's Garage when a smoke detector failed to operate. The court upheld this provision over challenges based on public policy arguments. The court found that there was no disparity of bargaining power since the provision permitted the customer to arrange

for greater service at a higher price "commensurate with the level of protection desired." The court attempted to articulate various economic public policy reasons for finding the provision enforceable, including concluding that the customer could have purchased insurance to protect its interests.

(3) Unconscionability. Whether a contract is unconscionable is a question of law for the court to decide. "*Unconscionability*" has no precise legal definition because it is not a concept but a determination to be made in light of a variety of factors. In general, the term "unconscionability" describes a contract that is unfair because of its overall one-sidedness or the gross one-sidedness of its terms. Although no single test exists to determine if a contract is unconscionable, two questions are generally asked: (1) How did the parties arrive at the terms in controversy; and (2) Are there legitimate commercial reasons which justify the inclusion of those terms? The first question, described as the procedural aspect of unconscionability, is concerned with assent and focuses on the facts surrounding the bargaining process. The second question, described as the substantive aspect of unconscionability, is concerned with the fairness of the resulting agreement. The court in *Arthur's Garage v. Racal-Chubb,* 997 S.W.2d 803 (Tex.App.-Dallas 1999, *no writ*) found that the *limitation of liability* provision and the *indemnity* provision were not unconscionable "considering the totality of the circumstances" citing *Pony Express Courier Corp. v. Morris*, 921 S.W.2d 817, 820 (Tex.App.-San Antonio 1996, *no writ*); *Wade v. Austin,* 524 S.W.2d 79, 85 (Tex.Civ.App.-Texarkana 1975, *no writ*); *Southwestern Bell Tel. Co. v. DeLanney,* 809 S.W.3d 493, 498-99 (Tex. 1991, Gonzalez, J. concurring op.); and *Leon's Bakery, Inc. v. Grinnell Corp.,* 990 F.2d 44, 49 (2nd Cir. 1993). *Also see* TEX. BUS & COMM. CODE §§ 2.302 *Unconscionable Contract or Clause* (Vernon 1994)(discussing unconscionable contracts under the Uniform Commercial Code) and 17.45(5) (Vernon Supp. 2002)(describing unconscionable actions under the Texas Deceptive Trade Practices - Consumer Protection Act); 1 J. White & R. Summers, UNIFORM COMMERCIAL CODE § 4-3 at 203 (3d ed. 1988); and RESTATEMENT (SECOND) OF CONTRACTS § 208, comment a (1979); Leff, *Unconscionability and the Code - The Emperor's New Clause,* 115 U. PA. L. REV. 485 (1967); and Mallor, *Unconscionability in Contracts Between Merchants,* 40 SW. L. J. 1065 (1986).

(4) Minors. It appears that a parent can not release, in advance, a minor child's right to recover for personal injuries caused by the negligence of another. In *Munoz v. II Jaz Inc. d/b/a Physical Whimsical*, 863 S.W.2d 207 (Tex. App.-- Houston [14th Dist.] 1993, *no writ*), the court held that a fact issue existed whether an adult sister of the nine-year-old minor plaintiff had been authorized by the parents to waive the minor's rights when the adult sister was permitted to take her sister to the amusement park. The adult sister signed a release for "any accidents occurring while on the property."

The court noted that the Texas Supreme Court has a "strong, long-standing policy to protect the interests of its children" and cited the concurring opinion of Justice Doggett wherein the Justice stated that parental releases of a minor child's potential claims are "outrightly disfavored." *Williams v. Patton*, 821 S.W.2d 141, 145 (Tex. 1991). *See also Fitzgerald v. Newark Morning Leger Co.,* 111 N.J. Super. 104, 267 557 (N.J. 1970)--holding that a release form signed by the parent as a condition of the child's participation in an outing sponsored by the defendant was void as against public policy; *Ferdor v. Mauwehu Council, Boy Scouts of America, Inc.*, 21 Conn. Supp. 38, 143 A.2d 466, 468 (Conn. Super. Ct. 1958)--holding that waiver of all claims for damages signed by the parent as a condition of the child attending summer camp was invalid as against public policy.

Query: What about the express negligence doctrine? *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993).

(5) Gross Negligence. The court in *Smith v. Golden Triangle Raceway*, 708 S.W.2d 574 (Tex. App.--Beaumont 1986, *no writ*) **struck down** a portion of a release that released the "releasee" (the race track) from liability for its gross negligence. This is the position of the Restatement. RESTATEMENT OF CONTRACTS § 574 (1932). The court cited various decisions from other jurisdictions supporting this conclusion.

The court upheld the release as to injuries due to the race track's negligence. The court found that this case did not involve an issue of unequal bargaining power. There is no public policy to protect a right to be a spectator on the infield of a race track. *Corpus Christi Speedway v. Morton,* 279 S.W.2d 903 (Tex. Civ. App.-- San Antonio 1955, *no writ*). The court in *Keszler v. Memorial Medical Center of East Texas*, 931 S.W.2d 61 (Tex. App.--Beaumont 1996, *no writ*) held that a release covering "all causes of action, whether sounding in tort or contract" could not as a matter of law based on public policy release a claim based on the gross negligence of the Released Party.

(6) Intentional Torts. The court in *Sedona Contrg. v. Ford, Powell,* 995 S.W.2d 192 (Tex.App.-San Antonio 1999, *no writ*) noted that consent can constitute a defense for liability for an intentional tort, and thus reasoned that a waiver as to future intentional torts may be enforceable under certain circumstances. Ford, Powell recommended that a school district accept the bid of the second lowest bidder, Sedona was the lowest bidder. The bid documents contained the following waiver:

Provision:

> By submitting a bid, each bidder agrees to waive any claim it has or may have against the Owner [NEISD], the Architect/Engineer, and their respective employees, arising out of or in connection with the administration, evaluation, or recommendation of any bid; waiver of any requirements under the Bid Documents; or the Contract Documents; acceptance or rejection of any bids; and award of the Contract.

The court noted that it had previously found *Golden Triangle* to be too broad in its application of the RESTATEMENT (SECOND) OF TORTS. In *Smith v. Holley,* 827 S.W.2d 433, 438 (Tex.App.-San Antonio

1992, *writ denied*) the court was faced with the issue of whether a prospective employee could release a previous employer from liability resulting from the communication of information regarding their work history. In its analysis, the court recognized the holding of *Golden Triangle*, but concluded that its application to intentional conduct was too broad. The court in *Smith* stated, "that it is universally recognized that in the right circumstances one can consent to certain actions that otherwise would be intentional torts." In *Smith* the court held Holley effectively consented to the possibility of defamation by signing a release form authorizing the release of work history. The court also cited *Unocal Corp. v. Dickson Resources, Inc.*, 889 S.W.2d 604, 610 (Tex.App.-Houston [14th Dist.] 1994, *writ denied*) holding that waiver, concerning oil and gas information, to be effective which permitted for the general waiver of future intentional tort claims and extinguished plaintiff's right to sue.

b. Mutuality. In *Sterling Computer Systems of Texas, Inc. v. Texas Pipe Bending Co.*, 507 S.W.2d 282 (Tex. Civ.App.--Houston [1st Dist.] 1974, *writ ref'd*) the court refused to enforce a contract due to its failure to have the requisite basic consideration merely because of the presence of the following provision in the contract:

> SCS (Sterling) shall not be liable for its failure to provide the services herein and shall not be liable for any losses resulting to the client (Texas Pipe Bending) or anyone else by reason of such failure.

Id. at 282. The court refused to imply an obligation on SCS to perform the contract. *See* 31 TEX. JUR.2d 238 § 91 *Contracts-Performance of agreement* (1994).

Similarly, in *Spellman v. Lyons Petroleum, Inc.*, 709 S.W.2d 295 (Tex. App.--Houston [14th Dist.] 1986, *writ ref'd n.r.e.*), the court refused to imply a reasonable effort to perform a contract which "contained no requirement that (Lyons Petroleum) make a reasonable effort to perform." *See*, however, *Fuqua v. Fuqua*, 528 S.W.2d 896 (Tex. Civ. App.--Houston 1975, *writ ref'd n.r.e.*) for a requirement of "good faith" or "reasonable efforts."

On the other hand, "**no personal liability clauses**" or "non-recourse obligations" are common and upheld. In *Duracon, Inc. v. Price*, 817 S.W.2d 147, 148 (Tex. App.--El Paso 1991, *writ den'd*), the court of appeals upheld the following no personal liability clause in a lease:

Provision:

> No personal liability is assumed under this Lease by Lessee or Assignee, except as may be otherwise agreed between the parties in writing.

The court determined that the landlord's sole recourse was to terminate the lease and for the tenant to lose the improvements it had built on the premises (a Ramada Inn).

c. Offer and Acceptance. As to existing claims to be released, a party must be aware of the claim being released and the claim must be sufficiently described in the release to be understood by the releasor as being released. *Victoria Bank & Trust Co. v. Brady*, 779 S.W.2d 893, 903 (Tex. Civ. App.--Corpus Christi 1989), *aff'd* 811 S.W.2d 931 (Tex. 1991).

A release is not valid if the Releasing Party has been induced to execute the release by fraud. *Texacadian Fuels, Inc. v. Lone Star Energy*, 896 S.W.2d 233 (Tex. App.--Houston [1st Dist.1995], *judgment vacated by agreement*, 922 S.W.2d 549 (Tex. 1996).

d. Typical Exculpations and Releases.

(1) Leases. The causes for which landlords frequently disclaim liability fall into three general categories, which include: (i) damages caused by the tenant; (ii) damages typically covered by insurance; and (iii) damages resulting from causes beyond the landlord's control.

It is fairly obvious as to why landlords disclaim liability for damages caused by the tenant. The landlord should not be penalized by some act of the tenant or other persons connected to or in the control of the tenant.

The second type of disclaimer includes those damages typically covered by insurance. These causes include the elements; the failure of equipment, pipes, and wiring; and the disruption of the tenant's business caused by repairs or alterations to the property necessitated by accidents.

The third category of disclaimer includes items viewed as not being within the landlord's control. For example, liability for damages caused by the acts of other tenants or adjacent property owners; damages caused by vandalism; and events of "*force majeure*." *See* for example, *Federated Department Stores, Inc. v. Houston Lighting & Power Co.,* 646 S.W.2d 509 (Tex. App. [1st Dist.] 1982, *no writ*) where a department store was unable to recover for lost profits due to interruptions in electrical service where the power supply contract contained a clause limiting liability to the cost of repair of physical damages caused by the power failure.

Another typical exculpation provision contained in large commercial centers is a provision exculpating the landlord from liability beyond its interest in the commercial center or by limiting recovery against the landlord to recovering a judgment lien against the landlord's interest in the commercial center without recourse to other assets of the landlord. The landlord's lender may insist upon such type of exculpation in order to give the lender comfort that if it becomes the owner of the center it is not exposing its assets to liabilities to the tenants. An issue may exist as to whether this type of exculpation clause must meet the fair notice requirements. Prudence dictates that all forms of exculpation, release, and waivers built into leases be both conspicuous and expressly reference that recovery for the negligence of the landlord as being exculpated, released or waived.

Similarly, an issue exists as to whether the standard waiver of subrogation needs to comply with the fair notice requirements (the express negligence test and the conspicuousness requirement).

See **Appendixes 5 and 6** for various typical waivers and exculpatory clauses in landlord-oriented leases.

(2) Construction Contracts. Like leases, construction contracts and subcontracts contain numerous clauses whereby one party disclaims liability and the other party waives or releases liability of the other party. Releases of recovery to the extent property damaged is covered by property insurance and waivers of subrogation are contained in the AIA standard construction documents. *See* **Appendix 11 Waiver of Recovery and Subrogation - AIA Forms A201 and A101**.

For example, in *Derr Constr. Co. v. City of Houston,* 846 S.W.2d 854 (Tex. App.--Houston [1st Dist.] 1992, *no writ*), the court held that a release/indemnity provision in a subcontract released the owner (the City of Houston) from liability for damages to the subcontractor's crane. The court held that the owner was a named third party beneficiary of the release in the subcontract. The court also held that the subcontractor's insurer could not assert any rights of subrogation to pursue the owner for the monies it had paid the subcontractor for damages to the crane. The provision in the subcontract reads as follows:

Provision:

> Subcontractor hereby assumes full responsibility and liability for the work to be performed hereunder, **and** hereby release, relinquishes and discharges **and** agrees to indemnify protect and save harmless Contractor, the City ... from all claims, demands and causes of action of every kind and character including the cost of defense thereof, for any injury to, including death of, person (**whether they be third person, contractor, or employees of either of the parties hereto**) and any loss of or damage to property (**whether the same be that either of the parties hereto or of third parties)** caused by or alleged to be caused, arising out of, or in connection with Subcontractor's work to be performed hereunder ... whether or not said claims, demands and causes of action in whole or in part are covered by insurance hereinbefore ... . (Court's emphasis in bold; author's emphasis underlined.)

Id. at 858. This case was decided after the court of appeals' decision in *Dresser Industries, Inc. v. Page Petroleum, Inc.* upholding the Houston Fishing Tool release provision, but before the supreme court's decision striking it down as not being conspicuous. The court did not address the conspicuousness of the provision in *Derr Construction.* Also, the court did not review the release in light of the express negligence test.

The court of appeals in *Valero Energy Corp. v. Kellogg Const. Co.*, 866 S.W.2d 252 (Tex. App.--Corpus Christi 1993, *writ denied*) **upheld** the following provisions waiving a contractor's liability for negligence, gross negligence or products liability and waiving the DTPA:

> 6.8 Owner shall release, defend, indemnify and hold harmless Contractor, its subcontractors and affiliates and their employees performing services under this Agreement against all claims, liabilities, loss or expense ... arising out of or in connection with this Agreement or the Work to be performed hereunder, including losses attributable to Contractor's negligence, to the extent Contractor is not compensated by insurance carried under this Article.
>
> 6.9 Neither Contractor nor its affiliates nor its subcontractors or vendors, either individually or jointly shall be liable to Owner or its affiliates, irrespective of whether alleged to be due to negligence or otherwise, for loss of anticipated profits or interest, for loss by reason of Plant shutdown or non-operation of the Plant or other equipment, for loss of catalysts or chemicals or for any consequential or special loss or damage arising from any reason whatsoever.

The Supreme Court in *Green International, Inc. v. Solis*, 951 S.W.2d 384 (Tex. 1997) held that the fair notice doctrine, used by the supreme court in *Dresser Industries, Inc. v. Page Petroleum, Inc.* 853 S.W.2d 505 (Tex. 1993) to deny enforcement to a "release" of liability for negligence occurring subsequent to the execution of the release, should not be extended to deny enforcement of a "**no damages for delay**" clause and a "**no consequential damages for wrongful termination**" clause.

The jury found that Green failed to timely deliver materials, failed to deliver properly fabricated materials, failed to provide proper access to the site, failed to coordinate or resolve conflicts between the work of other subcontractors and Solis, failed to timely submit shop drawings, and failed to resolve conflicts in plans and specifications. Because of these events, Solis incurred additional expenses and stopped work due to Green's failure to pay for such additional expenses.

The court stated

> This clause does not constitute the type of extraordinary risk-shifting found in *Dresser.* It is not an indemnity agreement because it does not shift Green's liability for third party claims to Solis... Also, this clause is not a release as defined in *Dresser* because it neither "extinguishes[es] the claim or cause of action" nor establishes "an absolute bar to any right of action on the released matter".
>
> The distinction between *Dresser* and this case lies in the fact that *Dresser* concerned the shifting of tort and negligence damages, whereas the no-damages-for-delay clause shifts economic damages resulting from a breach of contract. We noted in *Dresser* that most contract clauses operate to transfer risk in some way. ... However, we were concerned with clauses that operate to shift risk in an extraordinary way, such as exculpating a party from the consequences of its own future negligence. ... Here, the parties agreed that Solis would bear the risk that the projects would not be completed on time, even if Green caused the delay.....

Interestingly, Justice Gonzales, who had written the opinion of the court in *Dresser* extending the fair notice requirements to releases, is forced to dissent in *Green International*, because he is unable to find the

"distinction" between a release and the no-damages-for-delay clause litigated in *Green International.* Justice Gonzales stated

> This clause transfers all risk of delay damages to Solis. If operative, it relieves Green in advance of any liability for such damages and surrenders Solis's right to recover them from Green. In very plain language, it releases Green from any liability resulting from delays. I therefore disagree with the Court's conclusion that "this clause is not a release as defined in *Dresser*....
>
> Additionally, the delay-damages provision would exculpate Green in advance for delays caused by its own negligence. The only significant difference between this release and the one at issue in *Dresser* is that this release is broader. It is not limited to negligence, but may also be construed to absolve Green of liability for its own intentional acts that delay Solis's work. The policy underlying *Dresser's* imposition of fair-notice standards, which protect parties from waiving their right to recover for negligence, apples with even greater force here. Because the delay-damages provision meets *Dresser*'s definition of release, and because the same policy concerns arise regarding this particular risk- sifting provision, I would apply the two--part *Dresser* test to the facts of this case.

The court also noted that the public policy behind the fair notice requirement of "conspicuousness" was not as strong in a case where the parties were experienced contractors familiar with the industry custom of allocating risk for delays.

The provisions in question read as follows:

Provision: "No Damages for Delay"

> Contractor, except as provided for in this paragraph 8(a) and (b), shall not be liable to the Subcontractor for delay to Subcontractor's work by the act, neglect or default of the Owner, Contractor, or the Architect, or by reason of fire, act of God, riot, strike, action of workmen or others, or any cause beyond Contractor's control.
>
> (a) The Contractor will be liable to the Subcontractor for damages incurred as a result of any acts, or failures to act, by the Owner which delays the Work, only if and to the extent the Owner is liable and pays the Contractor for such damages.
>
> (b) Should Contractor delay Subcontractor in the work, Subcontractor shall receive an extension of time for completion equal to delay if a written claim is made within forty-eight hours, and under no circumstances shall Contractor be liable to pay to Subcontractor any compensation for such Contractor caused delays.

Provision: "No Damages for Wrongful Termination"

> Should subcontractor be wrongfully terminated under this Agreement, the Subcontractor shall be entitled only to be paid a pro-rata percentage of the total Subcontract price, equal to its percent of completion and not for anticipatory profit, damages, or consequential damages.

(3) Waiver of Workers' Compensation System. The court of appeals in *Beneficial Personnel Services of Texas, Inc. v. Porras*, 927 S.W.2d 177 (Tex. App.--El Paso 1996, *writ withdrawn and judgment vacated by settlement*) held that the following waiver by an employee of the benefits of the Workers' Compensation Act contained in an employment contract could **not** be enforced by the employer to limit liability to its employee for injuries:

Provision:

> 3. Worker's Compensation Benefits. BPS has agreed in the Personnel Lease Agreement with its Client Company to provide worker's compensation benefits provided by a non- admitted insurance carrier to Employee for injuries compensable under the Texas Worker's Compensation Act and similar acts of other jurisdictions (collectively referred to as the "Act") while Employee is assigned to Client Company and to waive (give up) their common law defensed [sic] against the Employee as set forth in the corresponding Act. In exchange, the Employee agrees to limit his/her recovery against BPS and Client Company for such compensable injuries to benefits allowed by the corresponding Act. These benefits are provided by a non- admitted insurance carrier.

The court held that this provision did **not** satisfy the express negligence test or the conspicuousness requirement of the fair notice test. The court labeled this provision as an "extraordinary shift of common-law liability outside the auspices of the state-sanctioned workers' compensation system." The court held that BPS' agreement to make certain limited payments in return for the release from negligence liability did not relieve BPS of its obligation to comply with the fair notice doctrine. The found that the employment agreement made "no mention of negligence, waiver of common law rights, or any other specific statement that the parties intended to waive liability for BPS's acts of negligence committed in the future." *Id.,* at 184.

e. Strict Construction. Since an exculpatory provision is drafted by the Released Party to release or carve out liabilities or contractual obligations from other expressed or implied duties, courts will strictly construe such provisions. Releases will be subject to the same rules of construction discussed above as to indemnity agreements. *See* the discussion of the rules used by courts to interpret indemnity agreements at **Article IIE Rules of Construction**.

(1) Scope of Release. Any claims not clearly within the subject matter of the release are not discharged. General categorical release clauses are narrowly construed. In *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414, 422 (Tex. 1984). *Vela v. Pennzoil Producing Co.*, 723 S.W.2d 199 (Tex.App.--San Antonio 1986, *writ ref'd n.r.e.*)--claims not clearly within subject matter of the release are not discharged, even if such claims existed at the time the

release was executed. In *Victoria Bank & Trust Co. v. Brady*, 811 S.W.2d 931, 938 (Tex. 1991), the supreme court held that a release executed by a borrower in a settlement agreement releasing a bank "from any and all claims and causes of action ... directly or indirectly attributable to the described loan transaction" did not include the borrower's claim of tortious interference by the bank in the borrower's contract with a third party arising out of the borrower's sale of an asset as to which the bank erroneously asserted a security interest.

The court in *Memorial Medical Center of East Texas v. Keszler,* 943 S.W.2d 433 (Tex. 1997) distinguished the release litigated in *Keszler* from the release litigated in *Victoria*. In *Keszler* Memorial and Keszler entered into a Compromise Settlement Agreement and a separate Release document concerning damage claims that Keszler asserted against Memorial due to Memorial's terminating staff privileges at the hospital. Keszler later sued the hospital for fraud, negligence, and gross negligence for injuries Keszler allegedly suffered due to exposure to ethylene dioxide, a toxic sterilizing agent the hospital used during his employment. The *Keszler* court found that the release language, releasing all as to "any other matter relating to [Keszler's] relations with [Memorial]", included "all" claims including claims of negligently caused injuries to Dr. Keszler. The court noted that the release in *Victoria* was limited to claims arising out of "the above described loan transaction", which loan transaction did not as it turned out include claims arising out of another loan transaction with Victoria Bank & Trust. The court also upheld the release as being effective to release Keszler's claim for gross negligence.

(2) A Continuum of Culpable Mental States. *See* the discussion at Article IIE2c(4) Indemnified Matters - Contractual Exceptions.

(a) "Negligence" versus "Intentional Acts". "Negligence" does not include intentional acts. *Richker v. Georgandis*, 323 S.W.2d 90 (Tex. Civ. App.--Houston 1959, *writ ref'd n.r.e.*).

(b) Exclusions for Gross Negligence. The issue of whether a release can cover future gross negligence has not been yet been decided by the Texas Supreme Court. The Supreme Court in *Memorial Medical Center of East Texas v. Keszler,* 943 S.W.2d 433 (Tex. 1997) upheld the "all claims" release as covering Keszler's claim for damages arising out of Memorial's alleged gross negligence by making a distinction for post-accident waivers of liability. The court stated

> The court of appeals held that such a release is against public policy. 931 S.W.2d at 63 (citing *Smith v. Golden Triangle Race*way, 708 S.W.2d 574, 576 (Tex.App.--Beaumont 1986, *no writ*)). However the court of appeals failed to distinguish a pre-accident waiver of liability from a post-injury release made in settlement of claims. In *Golden Triangle,* the issue was whether a pre-injury release could effectively dispense with a claim of gross negligence. *Id.* We have never held post-injury releases of gross negligence claims invalid. There is no logic in prohibiting people from settling existing claims. Significantly, such a rule would preclude settlement of many such claims. The court of appeals erred in holding that Keszler could not release his gross negligence claim against Memorial.

In *Franklin v. Marie Antoinette Condominium Owners Ass'n, Inc.,* No. B064293 Cal. App. Ct. 2nd App. Dist. (1993), a California appeals court held that a unit owner was not entitled to recover for water damage to her unit based upon an exculpatory clause in the condominium declaration. The clause barred the association from liability for property damage caused by a central plumbing leak unless the damage was caused by the gross negligence of the association or its directors. The unit owner sustained $74,000 in damages to her unit from water leaking into her unit through the HVAC vents. The court found that the exclusion from the exculpatory clause for "gross negligence" did not cover the omission of the association to prevent damage to the unit owner's unit. The court also held that enforcement of the clause was reasonable and fair to the condominium owners as a whole, since they had agreed to bear the risk of loss beyond what they could recover from the association's insurance policy.

(3) Conflicting Provisions Nullify Exculpation. An express duty paragraph and a separate exculpation paragraph have been held to nullify the exculpation provision. *Shintech, Inc. v. Group Constructors, Inc.*, 688 S.W.2d 144 (Tex. App.--Houston [14th Dist.] 1985, *no writ*).

(4) Parties Released.

(a) Named Specifically. In *McMillen v. Klingensmith*, 467 S.W.2d 193 (Tex. 1971), the court held that a release discharges only those tortfeasors that it specifically names or otherwise specifically indemnifies. The Texas Supreme Court in *Duncan v. Cessna Aircraft Co.*, 665 S.W.2d 414 (Tex. 1984) approved the decisions in *McMillen*, and in *Lloyd v. Ray*, 606 S.W.2d 545, 547 (Tex. Civ. App.--San Antonio 1980, *writ ref'd n.r.e.*) and *Duke v. Brookshire Grocery Co.*, 568 S.W.2d 470, 472 (Tex. Civ. App.-- Texarkana 1978, *no writ*) holding that the mere naming of a general class of tortfeasors in a release does not discharge the liability of each member of that class. A tortfeasor can claim the protection of a release only if the release refers to him by name or with such descriptive particularity that his identity or his connection with the tortious event is not in doubt.

Also see Angus Chemical Co. v. IMC Fertilizer, Inc., 939 S.W.2d 138 (Tex. 1997) where the court held that the release by an injured party of a tortfeasor does not release the tortfeasor's insurer; *Illinois Nat. Ins. Co. v. Pereez*, 794 S.W.2d 373 (Tex.App.--Corpus Christi 1990, *writ den'd*).

(b) "Agents" Do Not Include "Contractors". The release in *Doe v. Smithkline Beecham Corp.,* 855 S.W.2d 248 (Tex. App.--Austin 1993, *writ granted*) releasing Quaker Oats and its "agents" was held not to include a drug testing laboratory that was hired by Quaker Oats to perform pre-employment drug screens. The court held that the lab was an independent contractor and was not covered by the employment application release form that released "Quaker Oats, its employees and its agents,

from any liability based on the results of the drug screening." *See also Dresser Industries, Inc. v. Page Petroleum, Inc.,* 853 S.W.2d 505, 508-09 (Tex. 1993); *Summers v. Skillern & Sons, Inc.,* 381 S.W.2d 352, 356 (Tex. Civ. App.–Waco 1964, *writ dism'd w.o.j.*); *but cf. Getty Oil Co. v. Insurance Co. of North America,* 845 S.W.2d 794, 806 (Tex. 1992).

(5) Release of Unknown Claims. Release of future, unknown claims is permissible in Texas. *Sweeney v. Taco Bell, Inc.*, 824 S.W.2d 289, 292 (Tex. App.--Ft. Worth 1992, *writ denied*); *Pecorino v. Raymark Indus., Inc.*, 763 S.W.2d 561 (Tex. App.- -Beaumont 1988, *writ denied*)--release executed in settlement of claim by worker and wife against asbestos products manufacturers based on worker contracting asbestos released all claims, including those that might be discovered in the future, precluded subsequent action by worker's widow based on death of worker from mesothelioma.

(6) Inadvertently Released Matters. Although releases are to be construed narrowly, if the release is broad enough to cover the released claims, then the claim is released, even if the releasor is unaware of claim. *White v. Grinfas,* 809 F.2d 1157 (5th Cir. 1987)--the court held that a settlement and release agreement settling prior lawsuit, purported to waive all claims or losses between the parties, would not be set aside on the basis of mutual mistake because the plaintiff purchasers were unaware of structural defects in the foundation of the apartment project which was the subject of litigation between the parties. *See also Lubrizol Corp. v. Exxon Corp.,* 871 F.2d 1279 (5th Cir. 1992), *rehearing denied*, 964 F.2d 1145 (5th Cir. 1992), *cert. denied,* 113 S.Ct. 186 (1992)--phrase "any fact pleaded," as used in provision of settlement agreement in which plaintiff agreed that it would not assert "any claim or counterclaim" made in that action "or which could have been made based upon any fact pleaded," modified the phrase "which could have been made," rather than the previous clause concerning "any claim or counterclaim made;" release thus affected not only the claims actually raised in the suit, but all those that could have been made based on any fact pleaded. *See however*, Note, Mills, *Personal Injury Settlement Release are Avoidable on Grounds of Mutual Mistake: Williams v. Glash, 789 S.W.2d 261 (Tex. 1990),* 22 TEX. TECH LR. 309, 310 (1991).

C. "As Is". Absent an "***as is***" or similar clause, the seller of a product impliedly warrants that the product is merchantable, TEX. BUS. & COMM. CODE ANN. § 2.314 (Tex. UCC) (Vernon 1994), and that the product is fit for the particular purpose for which it is sold, *Id.* at § 2.315. Under the UCC "warranties" are designed to provide a remedy when a product fails to measure up to the seller's representations of quality. *Mid-Continent Aircraft Corp. v. Curry County Spraying Service, Inc.,* 572 S.W.2d 308, 313 (Tex. 1978); *Nobility Homes of Texas, Inc. v. Shivers,* 557 S.W.2d 77, 80 (Tex. 1977). Disclaiming warranties by an "as is" clause shifts the economic risk of product quality from the seller to the buyer. TEX. BUS. & COMM CODE ANN. § 2.316(c)(1)(Texas UCC) (Vernon 1994). *See* Annot., *Construction and Effect of Provision in Contract for Sale of Realty by Which Purchaser Agrees to Take Property "As Is" or in its Existing Condition*, 8 A.L.R. 5th 312, 373-79 (1992); Weintraub, *Disclaimer of Warranties and Limitation of Damages for Breach of Warranty Under the UCC*, 50 TEX.L.REV. 60 (1973). Baggett and Nolan, *Use of Disclaimers: "As Is Where Is Provisions*, 29th ANNUAL MORTGAGE LENDING INSTITUTE (UNIV. TEX. 1995); Alderman, *Current Status of DTPA Waivers, "As Is Transactions and Representations and Warranties,* 18th ANNUAL ADVANCED REAL ESTATE LAW COURSE R (1996).

The Texas Supreme Court recently upheld the use of "as is" clauses as a means of risk management in *Prudential Ins. Co. of America v. Jefferson Associates, Ltd.*, 896 S.W.2d 156 (Tex. 1995). In *Prudential* the buyer recognized that it was neither relying upon materials provided by the seller nor a misstatement by the seller's agent as to the character of the building being purchased. The court held:

> A valid "as is agreement, like the one in this case, prevents a buyer from holding a seller liable if the thing sold turns out to be worth less than the price paid because it is impossible for the buyer's injury on account of this disparity to have been caused by the seller .... The sole cause of a buyer's injury in such circumstances, by its own admission, is the buyer himself He has agreed to take the full risk of determining the value of the purchase. He is not obligated to do so; he could insist instead that the seller assume part or all of the risk by obtaining warranties to the desire effect. If the seller is willing to give such assurances, however, he will ordinarily insist upon additional compensation. Rather than pay more, a buyer may choose to rely entirely on his own determination of the condition and value of his purchase. In making this choice, he removes the possibility that the seller's conduct will cause him damage ....
>
> Justice Cornyn's concurring opinion argues that Goldman's "as is" agreement is relevant to whether Prudential caused him harm, but not controlling. If Goldman's position at trial were the same as the position he took in the 'as is' agreement, he could not recover on any of the theories he asserts. Unable to show any reason why the agreement should not be enforced, such as fraudulent inducement, Goldman ought to be held to his voluntary, freely negotiated affirmation of his own assessment of the building. Justice Cornyn's concurring opinion suggests that Prudential should prevail if this was an arm's-length transaction. Goldman does not dispute that it was.

Id., at 161-62.

1. Relevant in Apportioning Liability for Third Party Injuries. An "***as is***" clause is not the equivalent of an effective indemnity or release, but may be some evidence to be considered by the jury in apportioning negligence liability between the seller and purchaser of personal property for injuries caused by condition of the personal property. In *Folks v. Kirby Forest Ind. Inc.*, 10 F.3d 1173 (5th Cir. 1994), the court of appeals found that the district court committed an error in advising the jury that the jury should not consider the "as is" terms of the sale in assessing liability between Kirby and Hood Industries, Inc. In

Kirby Forest, an employee of Knight's Machinery Removal was injured when a machine collapsed due to the lack of hydraulic fluid. Kirby Forest had sold the machine "as is" to Hood Industries, Inc. at an auction at Kirby's closed plywood plant. After Hood Industries bought the machine, it hired Knight Machinery Removal to remove the machine and reinstall it in Hood Industries' sawmill. Kirby Industries was liable for injuries to Knight Machinery Removal's employee, as the employee was an invitee injured by a condition existing on Kirby's premises. *Id.* at 1176 applying the Restatement (Second) of Torts § 343 (1965) adopted in Texas in *Adam Dante Corp. v. Sharpe,* 483 S.W.2d 452, 454- 55 (Tex. 1972), and rearticulated in *Corbin v. Safeway Stores, Inc.,* 648 S.W.2d 292 (Tex. 1983) and *Keetch v. Kroger Co.,* 845 S.W.2d 262, 266 (Tex. 1992).

The court noted that *Kirby* did not contend that the "as is" clause reformed an otherwise defective indemnity clause. *Id.* 1180 n.14. However, the court also rejected the dissent's view that the court had changed the "as is" clause into an indemnity by permitting its presence in the sales contract to be considered by the jury as some evidence in apportioning liability between seller and buyer as to responsibility for the plaintiff's injury. *Id.* at 1180 n.16, and 1181 n.19.

2. Not Effective to Escape Environmental Liability. An "as is" disclaimer in a sales contract will not shield the seller from liability to the buyer for contributing towards environmental cleanup response costs under CERCLA, 42 U.S.C. § 9607(a)(4)(B). *See Channel Master Satellite Sys. v. J.F.D. Electronics,* 702 F. Supp. 1229 (E.D. N.C. 1988). *Also see Southland Corp. v. Ashland Oil, Inc.* 696 F. Supp 994 (D.N.J. 1988)--"as is" clause does not bar CERCLA claims; *Allied Corp. v. Frola,* 730 F. Supp. 626 (D.J.J. 1990)--"as is" clause does not bar common law strict liability claims. *See generally* Clark, *Continued Liability of Seller After a Sale of Producing Oil and gas Properties,* 41 INST. ON OIL & GAS L. & TAX'N 5-1, 5-23 (1990)--discussing impact of an "as is" clause on environmental liabilities.

See the discussion of provisions negating buyer's reliance on information or disclosures provided by a seller in an "as is" contract in Pierce, *Structuring Routine Oil and Gas Transactions to Minimize Environmental Liability*, 33 WASHBURN L. J. 76, 112-119 (1993). The allocation of environmental risks in a sales transaction through representations, warranties, and indemnities will generally result in a contractual assumption of liability. In cases where a condition is known to exist, a preferable method may be to provide for an express assumption of liability.

Drafting: Baggett and Nolan, *Use of Disclaimers: "As Is Where Is Provisions*, 29th ANNUAL MORTGAGE LENDING INSTITUTE (UNIV. TEX. 1995).

An environmental indemnity agreement may be employed to shift back to the seller a potential cleanup risk arising out of detected marginal contaminations below reportable levels, but significant enough to trigger agency action if the condition comes to the attention of the governmental agency.

3. Fraud and Oral Statements. Of course, an "as is" clause cannot protect a seller from fraud or material omissions. The court in *Gopher Oil Co. v. Union Oil Co.,* 955 F.2d 519 (8th Cir. 1992) found that an "as is" clause was ineffective in preventing a buyer from obtaining relief from a seller whose employees had oral statements as to prior occurrences at the property, but had omitted to mention a material hazardous substance spill. *See* RESTATEMENT (SECOND) OF CONTRACTS § 161 (1981) providing "A person's non- disclosure of a fact known to him is equivalent to an assertion that the fact does not exist in the following cases only: ..." *Also see Smith v. Levine,* 911 S.W.2d 427 (Tex. App.–San Antonio 1995, *writ denied*) as to fraud by oral misrepresentations.

4. May Not Be Effective to Escape DTPA Liability. Furthermore, the "consumer" has the right to complain that the contract was "unconscionable," *see e.g., Wyatt v. Petrila,* 752 S.W.2d 683 (Tex. App.--Corpus Christi, *writ denied*), and complain of independent affirmative misrepresentations made by the seller that would not otherwise constitute actionable fraud, *see e.g., Weitzel v. Barnes,* 691 S.W.2d 598 (Tex. 1985). An effective waiver of the DTPA would address both of these issues. Texas Deceptive Trade Practices- Consumer Protection Act, § 17.42 TEX. BUS. & COMM. CODE ANN. (Vernon 1997); *see Valero Energy Corp. v. Kellogg Const. Co.,* 866 S.W.2d 252 (Tex. App.--Corpus Christi 1993, *writ denied*).

5. DTPA Waivers. Effective September 1, 1995, the Texas Deceptive Trade Practices Act was amended. These amendments added several exceptions to the coverage of the Act. One of these exceptions is for large commercial transactions. Section 17.49(f) and (g) provides that the Act does not apply to contracts in the following instances:

(1) transactions, a set of transactions, or projects involving a total consideration of more than $100,000, if the contract is written, the consumer is represented by legal counsel, and the transaction does not involve the consumer's residence; an

(2) a transaction, a set of transactions, or project involving a total consideration of more than $500,000, other than a transaction involving a consumer's residence (in this $500,000 exception, there is no requirement that the consumer be represented by legal counsel).

The 1995 amendments also simplified the **means to waive the Act**. Under the amended provision, a consumer may waive the Act if: the waiver is in writing and signed by the consumer; the consumer is not in a significantly disparate bargaining position; and the consumer is represented by legal counsel in seeking or acquiring the goods or services. These amendments eliminated the requirement that the consumer's attorney also sign the waiver and eliminated the special provisions applicable to business consumers. The waiver is not effective if the consumer's counsel was directly or indirectly identified, suggested or selected by a defendant or an agent of the defendant. The waiver must be conspicuous and in bold-face type of at least 10 points in size. It also must be identified by the heading "Waiver of Consumer Rights", or similar

language, and include language substantially the same as that provided in § 17.4(c)(3).

The most significant definition changed by the 1995 amendments is that of "unconscionability". The 1995 amendments eliminated Section 17.45(5)(B) which included within the meaning of "unconscionability" an act or practice which "results in a gross disparity between the value received and consideration paid, in a transaction involving transfer of consideration". Thus, unconscionability may only be established by showing an act or practice that takes advantage of a consumer's lack of ability, experience, or capacity to a grossly unfair degree. The amendments also clarified the definition of "knowingly" to indicate that the relevant time is the time the act or practice complained of occurred. The amendments added definitions for "economic damages" and "intentionally".

D. Limitation of Liability Provisions.

1. Distinguished from Exculpation Provisions and Releases. Unlike exculpatory provisions and releases, limitation of liability provisions merely limit one party's liability to a predetermined amount or type of allowed liability. Like exculpatory provisions and releases, a limitation of liability provision is a device used by the parties to manage risk and to allocate loss due to the occurrence of the risk. In a sense a provision setting a limitation of liability is like a liquidated damage provision. 5 CORBIN ON CONTRACTS § 1068.

Since limitation of liability provisions do not relieve a party of all risk, some courts have been willing to uphold such type provisions where they otherwise would not uphold a complete shifting of risk by use of a release or exculpatory provision. *See Drazek v. Mountain River Tours, Inc.* 884 F.2d 163 (4th Cir. 1989); *Lago v. Krollage,* 535 N.E.2d 107 (1991); *Galigan v. Arovitch,* 219 A.2d 463 (Pa. 1966); *Evens v. Texas Pacific-Missouri Terminal R.R.,* 134 F.2d 275 (5th Cir. 1943), *cert. den.* 319 U.S. 756, 87 L.Ed. 1709, 63 S.Ct. 1175 (1943); *Lumar Marine, Inc. v. Insurance Co. of North America*, 910 F.2d 1267 (5th Cir. 1990).

The use of limitation of liability provisions in construction or design contracts is statutorily recognized in Texas. TEX. CIV. PRAC. & REM. CODE § 130.004 (Vernon) provides that it does not prohibit or make void or unenforceable a covenant or a promise to do the following:

> Allocate, release, liquidate, limit or exclude liability in connection with a construction contract between an owner or other person for whom a construction contract is being performed and a registered architect or registered engineer.

2. Rationale for Use. A limitation of liability provision may be a suitable contractual risk shifting device where the profit to be obtained in a transaction is otherwise outweighed by a high potential for risk of enormous liability. In *Markborough California, Inc. v. Superior Court,* 277 Cal. App.3d 705, 277 Cal.Rptr. 919 (Cal. 1991) a designer of a lake facing a $5,000,000 potential limited its liability to its fee of $67,000.

3. Types. Limitation of liability provisions fall into two categories: provisions limiting the amount of damages to a predetermined or predeterminable amount and provisions limiting the type or characterization of damages recoverable.

a. Limitation of Amount of Liability. The most widely used type of limitation of liability provision is in limiting the amount of damages recoverable. The following is a limitation of liability provision suggested as an alternative provision by the American Institute of Architects for use by Architects in architect service agreements.

Provision:

> 12.2.1 COMPENSATION. Neither the architect, the architect's consultants, nor their agents or employees shall be jointly, severally or individually liable to the owner in excess of the compensation to be paid pursuant to this agreement or of _____ Dollars ($___), whichever is greater, by reason of any act or omission, including breach of contract or negligence not amounting to a willful or intentional wrong.

AIA Document B511, Guide to Amendments to AIA Document B141 (1993 ed.). In *Baker v. Roy H. Haas Assoc.s, Inc.,* 629 A.2d 1317 (Md.App. 1993) the court enforce a limitation of liability provision in a home inspection contract that limited an inspector's liability to the amount of its fee. The court upheld limiting the owner's recovery for his $2,000 in damages to the amount of the inspector's $250 fee on the basis that the inspector's negligence was not gross or willful, the bargaining positions of the parties was relatively equal, and the transaction did not involve a matter of public interest.

Similarly, the amount of damages can be limited to the amount payable under available insurance.

Provision:

> 12.2.1 INSURANCE. Neither the architect, the architect's consultants, nor their agents or employees shall be jointly or individually liable to the owner in any amount in excess of the currently maintained professional liability insurance coverage carried by the architect.

AIA Document B511, Guide for Amendments to AIA Documents B141 (1993 ed.).

A hybrid provision is a provision allowing the other party to choose either to limit liability to the professional fee being paid to the service provider or providing an alternative higher fee, thus allowing the professional some compensation for the increased risk and funds with which to protect against the increased risk by purchasing insurance. The following provision was upheld in *Georgetown Steel Corp. v. Union Carbide Corp.,* 806 F.Supp. 74 (D.SC 1992, *reversed on other grounds* ___ F.2d (4th Cir. 1993).

Provision:

Our liability for any damage on account of any error, omission or other professional negligence will be limited to a sum not to exceed $50,000 or our fee, whichever is greater. In the event the client does not wish to limit our professional liability to this sum, we agree to waive this limitation upon receiving client's written request, and an agreement by the client to pay additional consideration of four percent (4%) of our total fee or $200.00 whichever is greater.

b. Limitation of Type of Damages. Other limitation clauses limit the type of damages a party may recover by waiving certain types of damages, for example waiving any right to consequential damages. *See Florida Power and Light Co. v. Mid- Valley, Inc.,* 763 F.2d 1316 (11th Cir. 1985); *Long Island Lighting Co. v. IMO Delaval, Inc.,* 668 F.Supp. 237 (S.D. NY 1987); *Gibbes, Inc. II v. Law Engineering, Inc.,* U.S. App. Lexis 7602 (4th Cir. 1992). An example of this type of provision is the following provision.

Provision:

Except as expressly provided in this Agreement, neither party shall be liable for any special, indirect, incidental or consequential damages of any nature, including, without limitation, loss of actual or anticipated profits or revenue, loss by reason of shutdown, loss of use or interest, nonoperation or increased expense of manufacturing or operation or any costs, labor, or materials required for reconstruction or repairs. Contractor's aggregate liability arising from this Agreement, regardless of the theory of recovery, including breach of contract or negligence, shall not exceed the scope and limits of insurance required to be maintained in this Agreement, except this aggregate liability limit shall not apply to claims arising from damages caused by Contractor's gross negligence, willful acts or misconduct.