

INDEMNITY AGREEMENTS

Washington Public Ports Association – Annual Meeting

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2:10 – 3:00 PM

Presented by

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Introduction

Basics

- **Indemnity** is an undertaking by one party to compensate a counterparty for certain costs and expenses, typically stemming from third-party claims. **Indemnity provisions** appear in nearly all commercial agreements and are one of the most commonly and heavily negotiated provisions in a contract.
 - An essential risk allocation tool that allows parties to:
 - Customize the amount of risk they're willing to undertake (e.g., liability caps, materiality qualifiers, liability baskets);
 - Protect from damages and lawsuits more efficiently borne by a counterparty; and
 - Recover certain types of losses (e.g., attorney's fees).
 - A typical indemnification clause consists of separate and distinct obligations to (1) **indemnify** and (2) **defend**.

What's Dillon's Rule?

- **Dillon's Rule** says that municipalities have only the powers expressly granted by the legislature or necessarily implied by statute.
 - A conservative interpretation of powers by courts
 - Applies to special purpose districts, second class cities, and towns
- In Dillon's Rule jurisdictions, if the state doesn't delegate to a local government the authority to adopt a particular policy, a locality's adoption of that policy is void.

Validity of and Authority to Enter Indemnity Agreements

- No single case sets forth an exact test or specific set of requirements addressing the validity of indemnity agreements benefitting governmental entities. However, courts have upheld such agreements without specifically addressing authority to indemnify.
- Cases examining the subject have emphasized the following:
 - Specific sources of authority to contract.
 - Statutory construction and interpretation that best advances a statute's objects and purposes.
 - The parties' clearly expressed and unequivocal intent.
 - Public policy.

Selected Case Studies and Authority

- N. Pac. Ry. Co. v. Sunnyside Val. Irrigation Dist., 85 Wn.2d 920, 540 P.2d 1387 (1975)
 - In this case, both the Court of Appeals and Washington Supreme Court respected the validity of the indemnity agreement. Both courts had the opportunity to rule that indemnity agreements were unenforceable against counties but did not do so. This suggests a willingness to uphold indemnification agreements benefitting governmental entities.
- Barendregt v. Walla Walla Sch. Dist. No. 140, 26 Wn. App. 246, 611 P.2d 1385 (1980)
 - In the absence of a specific statutory authority to indemnify, a state or local government may not so contract.
- AGO 2006 No. 11 – May 3, 2006, n.4
 - The AGO distinguished *Barendregt* when discussing the authority of municipalities under Chapter 39.34 RCW, the Interlocal Cooperation Act, noting that the Court “as not addressing the authority to contract under RCW 39.34—it was addressing the authority of a state administrative agency; most importantly, it was not addressing a contract under a statutory provision such as RCW 39.34.180, which was intended to require the parties to consider all fiscal impacts of allocating the criminal justice administration.”

Selected Case Studies and Authority

- Washington Pub. Util. Districts' Utilities Sys. v. Pub. Util. Dist. No. 1 of Clallam Cnty., 112 Wn.2d 1, 771 P.2d 701 (1989)
 - Public utility districts have the requisite authority to enter into self-insurance agreements allowing indemnification of its officers and employees against direct claims by the port district itself.
 - Ports have the same statutory authority under RCW 53.08.208 (near-identical statute) as PUDs have under RCW 54.16.097.
- Washington Hosp. Liab. Ins. Fund v. Pub. Hosp. Dist. No. 1 of Clallam Cnty., 58 Wn. App. 896, 795 P.2d 717 (1990)
 - The Court of Appeals relied on the above PUD case to conclude that indemnity can occur in a direct (two party) action in a similar case involving a public hospital district, even though indemnification obligation of insureds ordinarily contemplated claims by third parties.
 - The Court also used the PUD case to dispose of the hospital insurer's argument that such indemnification would be an unconstitutional gift of public funds. Good faith rendering of services constitutes consideration, removing the case from the realm of "gifts" prohibited by Washington's constitution. See n.1.

Selected Case Studies and Authority

- City of Tacoma v. City of Bonney Lake, 173 Wn.2d 584, 269 P.3d 1017 (2012)
 - Here, the Court upheld the City of Tacoma's indemnification of other municipalities without specifically addressing its authority to indemnify.
- Snohomish Cnty. Pub. Transp. Benefit Area Corp. v. FirstGroup Am., Inc., 173 Wn.2d 829, 271 P.3d 850 (2012)
 - This decision came a month after *City of Tacoma* above. Once again, the court doesn't address the authority to indemnify but nonetheless upholds the agreement.
 - The central issue was whether the indemnity agreement clearly and unequivocally demonstrated the parties' intent that the commuter bus company would be required to indemnify the public transit authority for losses resulting from the public transit authority's own negligence.
 - **“To the extent allowed by law.”** The Court explained that the only time public policy has barred such indemnification is when the legislature has declared in specific circumstances that such indemnification is barred, using RCW 4.24.115 as an example.

Can Ports Provide Indemnification in Agreements?

Takeaways:

- **“It depends.”** There’s no case law setting forth exact test or specific set of requirements addressing the validity of indemnity agreements benefitting governmental entities. That said, the cases demonstrate a clear willingness by courts to respect and uphold such agreements.
- **Understand statutory authority applicable to your entity.** When drafting and negotiating indemnity provisions, ensure your entity’s authority to indemnify was either expressly granted by the legislature or can be necessarily implied by statute.
- **“To the extent allowed by law.”** Generally, parties may incorporate into a contract any provision that isn’t illegal or against public policy. Understand the limitations on indemnity imposed by the legislature in specific contexts (*e.g.*, construction) and draft indemnity provisions that reflect the clear and unequivocal intent of the parties as to the scope of indemnification.

Roundtable Discussion: Jay Donovan

Practical Benefits of Various Indemnification Provisions



Practical Considerations

- Indemnification Rights v. Insurance Rights
 - Expressly state that the availability of insurance does not, in any way, impact obligations under the Indemnification Provision.
 - Provides added protection if insurance coverage is denied.
 - Provided added protection if policy is exhausted.
 - Duty to “defend” – Diverging interests and the right to recover fees for personal counsel.

Practical Considerations

- Enforcing Indemnification Provisions:
 - Include an Attorney's Fee Provision
 - Tri-M Erectors v. Drake, 27 Wn. App. 529, 539, 6178 P.2d 1341 (1980) (indemnification provision must have express language providing for recovery of legal fees incurred establishing right to indemnification).
 - Jones v. Strom Construction Co., 84 Wn.2d 518, 523, 527 P.2d 1115 (1974) (“The general, and virtually unanimous rule appears to limit the allowance of such fees to the defense of the claim indemnified and not to extend such allowance for services rendered in established the right to indemnification. We hold, therefore, that, in the absence of express contractual terms to the contrary, an indemnitee may not recover legal fees incurred in establishing his right to indemnification.”).
 - ADR: Mediation / Binding Arbitration

Practical Considerations

- Simplicity & clarity are KEY
- Indemnification provisions are not “One Size Fits All” or “Hand-Me-Downs”

Conclusion

Questions?



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