Wisconsin Ready Mixed Concrete Association

CONTRACTUAL INDEMNITY CLAUSES:

A REFERENCE GUIDE

Prepared By

MWL

MATTHIESEN, WICKERT & LEHRER, S.C.
ATTORNEYS AT LAW

I. INDEMNITY CLAUSE BASICS

Indemnity clauses in construction contracts may cause concern for many subcontractors and material suppliers. The clauses often require subcontractors and material suppliers to take financial responsibility for, or reimburse, the general contractor ("GC") or owner for any loss that occurs during the performance of the contract, regardless of who actually caused the loss. The purpose of this reference guide is to give members of the Wisconsin Ready Mix Concrete Association a general understanding of the indemnity clauses that are frequently found in construction contracts, as well as the tools to identify some unfavorable consequences of these clauses. The following terms commonly appear in indemnity clauses:

- **Indemnity**: Requires one party to pay the other party for any damages regardless of who is at fault.
- **Indemnitor**: The party who assumes the obligation to pay the damages. This is usually referring to the subcontractor or material supplier.
- **Indemnitee**: The party who receives the benefit of not having to pay damages or is reimbursed for the damages. This is usually referring to the general contractor or owner.
- **Hold Harmless**: Prohibits one party from holding the other party responsible for damages regardless of who is at fault.
- **Negligence**: A legal term meaning failure to use reasonable care, resulting in damage or injury to another.
- **Willful Misconduct**: Intentionally violating a reasonable and uniformly enforced rule or policy.
- **Defend or Defense Costs**: All expenses to defend a claim or a lawsuit against a party, including but not limited to lawyers, investigation, fact gathering, experts, filing fees and court costs.
- **Liable or Liability**: Causing a violation of a person's right or failure to perform a legal duty that results in damage or injury.

Indemnity clauses are often woven together with hold harmless clauses due to their similarities. An example of such clause reads as follows:

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

These types of clauses cause an obvious wrong when the GC/owner is solely liable for a loss because it requires the subcontractor or material supplier to be financially responsible for the loss and prohibits the subcontractor or material supplier from making a claim against the GC/owner. GC/owners have historically insisted that subcontractors and material suppliers agree

to the indemnity clauses in a contract if they want to get the work. This affords GC/owners a superior bargaining power and ability to take advantage of subcontractors and material suppliers with an inferior power.

II. WISCONSIN INDEMNITY CLAUSES

Wisconsin enacted a statute that prohibits construction contracts from containing clauses that limit or eliminate liability for any damage or injury. Wisconsin statute § 895.447 provides:

> "Any provision to limit or eliminate tort liability as a part of or in connection with any contract, covenant or agreement relating to the construction, alteration, repair or maintenance of a building, structure, or other work related to construction, including any moving, demolition or excavation, is against public policy and void."[1]

However, this statute does not make all indemnity and hold harmless clauses void and unenforceable.[2] Since this statute limits both parties' right to choose the terms of their contract, Wisconsin courts will only make these clauses unenforceable when the clause actually limits or eliminates the liability of the GC/owner, rather then just shifts the financial responsibility to the subcontractor or material supplier.[3]

A. Formal Requirements

Wisconsin courts will apply general contract law requirements to indemnity and hold harmless clauses in construction contracts. The language of the indemnity clause is where a court will begin its analysis regarding the enforceability of the clause.[4] Clauses in construction contracts must be "conspicuous," or written in a way that's visible to the subcontractor or material supplier.[5] Additionally, indemnity clauses cannot be "unconscionable." Courts may find an indemnity clause is unconscionable when the subcontractor or material supplier had no meaningful choice in its terms and the clause is unreasonably favorable to the GC/owner.[6]

- A clause that says a subcontractor or material supplier must "indemnify" a GC/owner for any loss is enforceable, but a clause that says the subcontractor or material supplier will assume "liability" for a loss is not.
- A clause that requires a subcontractor or material supplier to indemnify the GC/owner for the GC/owner's own negligence is enforceable, but only if there is a specific and express statement saying the subcontractor or material supplier will "indemnify" the GC/owner for its own negligence.[7]

[1] Wis. Stat. § 895.447(1).
[2] *See Dykstra v. Arthur G. McKee & Co*., 100 Wis.2d 120, 301 N.W.2d 201 (Wis. 1981).
[3] *See Gerdmann by Habush v. U.S. Fire Ins. Co*., 350 N.W.2d 730 (Wis. Ct. App. 1984).
[4] *Fabco Equipment, Inc. v. Kreilkamp Trucking, Inc*., 352 Wis.2d 106, 841 N.W.2d 542 (Wis. Ct. App. 2013).
[5] Wis. Stat. § 402.302.
[6] Wis. Stat. § 401.201(10).
[7] *Spivey v. Great Atl. & Pac. Tea Co.*, 79 Wis.2d 58, 63, 255 N.W.2d 469, 472 (Wis. 1977).

B. Apportionment of Damages

Indemnity clauses can be categorized by whose negligence the clause requires the subcontractor or material supplier to indemnify for. There are three types of indemnity clauses:

1. Limited: Subcontractor assumes only the responsibility for its own negligence – if it is solely at fault. Wisconsin allows this type of indemnity clause.

2. Intermediate: Subcontractor assumes responsibility for its own sole negligence or partial negligence. If the GC/owner is solely at fault, there is no indemnity. Wisconsin allows this type of indemnity clause. There are two types of intermediate indemnity:

    a. Full indemnity: If the subcontractor is partially at fault, he pays all the damages. A GC/owner who was 99% at fault will receive indemnity from the subcontractor who was only 1% at fault.
    b. Partial Indemnity: Indemnity is on a sliding scale based on the extent of the subcontractor's negligence. This sets a cap on the amount of indemnity that can be had. If the GC/owner is 51% at fault, it is indemnified only for 49% of the total damages.

3. Broad: Subcontractor assumes all responsibility regardless of who is at fault, and indemnifies the GC/owner for the GC/owner's sole negligence, the subcontractor's sole negligence, and any joint negligence of the two. The entire risk of loss is transferred to the subcontractor. Wisconsin allows this type of indemnity clause, but only if the clause contains a specific and express statement requiring the subcontractor or material supplier to indemnify for the GC/owner's sole negligence.

III. INSURANCE REQUIRMENTS AND ISSUES

A. Liability Insurance

Wisconsin courts commonly enforce liability insurance requirements in various types of contracts based on the right of the parties to contract freely.[8] In a limited circumstance, the Wisconsin Supreme Court has determined that the specific and express statement requirement regarding the indemnitee's own negligence is not necessary when an insurance requirement is coupled with a hold harmless clause.[9] This would result in the subcontractor or material supplier having to indemnify the GC/owner for their own negligence without this specific statement in the clause. However, the placement and wording of the insurance requirement is extremely important. If the requirement to obtain liability insurance comes before the requirement to hold the GC/owner harmless in the clause, the GC/owner may be entitled to indemnification for its

[8] *See Herchelroth v. Mahar*, 36 Wis.2d 140, 153 N.W.2d 6 (Wis. 1967); *Hastreiter v. Karau Bldgs.,Inc*., 57 Wis.2d 746, 205 N.W.2d 162 (Wis. 1973).
[9] *See Id.*

own negligence without requiring a specific and express statement.[10] An example of this language reads as follows:

> "The Subcontractor agrees to secure and pay for liability insurance covering any loss arising out of the performance of the contract and hold the Owner, General Contractor, or its agents and employees, harmless."

B. Naming Additional Insureds

A construction contract may also require a subcontractor or material supplier to add the GC/owner as an additional insured.[11] Again, the language of the clause requiring addition of the GC/owner is important. If the clause requires the subcontractor or material supplier to name the GC/owner on their insurance policy, but does not have a specific or express statement regarding coverage for the GC/owner's own negligence, then a loss due to the GC/owner's negligence may not require indemnification.[12] Also, requiring the subcontractor or material supplier to add the GC/owner as an "additional insured" does not necessarily mean their name must be added to the policy.[13] It may be sufficient if the policy itself automatically adds people or entities when the subcontractor or material supplier enters a contract with them. It is important to check the language of the insurance policy regarding additional insureds.

C. Coverage for Contractually-Assumed Liability

It is not uncommon for an insurance policy to have an exclusion for contractually-assumed liability. The Wisconsin Supreme Court has analyzed the meaning of "contractually-assumed liability" and the types of liabilities that fit its definition.[14] The Court found the phrase specifically includes indemnity and hold harmless clauses since the clauses would require an insured to take financial responsibility for a third party's negligence, a risk an insurer cannot reasonably foresee. As such, it is also important to check the exclusions of the insurance policy to verify whether or not "contractually-assumed liability" is excluded.

IV. DUTY TO DEFEND

Some contracts will provide that the indemnitor must defend the indemnitee from claims or suits related to the contract. The duty to defend is similar to indemnification, but the two are separate and distinct under Wisconsin law.[15] A subcontractor or supplier's promise to defend creates an obligation to provide the other party with a legal defense against claims of liability

[10] *See Herchelroth*, 36 Wis.2d 140, 153 N.W.2d 6; *See also Sutton v. A.O. Smith Co*., 165 F.3d 561 (7th Cir. 1999).
[11] *See Campion v. Montgomery Elevator Co*., 172 Wis.2d 405, 493 N.W.2d 244 (Wis. Ct. App. 1992); *Fabco Equipment*, 2013 WI App 141 at ¶ 17.
[12] *See Campion*., 172 Wis.2d 405, 493 N.W.2d 244.
[13] *Fabco Equipment*, 841 N.W.2d 542 (2013).
[14] *American Family Mut. Ins. Co. v. American Girl, Inc*., 268 Wis.2d 16, 673 N.W.2d 65 (Wis. 2004).
[15] *Hamlin, Inc. v. Hartford Acc. and Indem. Co.*, 86 F.3d 93 (7th Cir. 1996).

within the scope of the indemnity clause. The following is an example of language which may impose a duty to defend:

> "The Subcontractor agrees to defend Owner against any and all claims, demands, and judgments, including attorney's fees, with legal counsel acceptable to Owner, and Owner shall have the authority for the direction of the defense."

A. Triggering and Scope of the Clause

The specific language of the contract will determine the scope of which claims the indemnitor must defend and *who* they must defend.[16] The next step is to determine whether the allegations of the claim brought against the indemnitor arguably fall within that scope.[17] The indemnitor becomes obligated to honor its duty to defend when the indemnitee "tenders" a claim against it for acts or omissions that are arguably within the scope of the agreement.[18] In this way, the duty to defend is broader than the duty to indemnify. It is triggered by claims that *arguably* fall within the terms of the contract, as opposed to an *actual* duty to indemnify, and the duty to defend is determined by what is alleged in the claim, rather than the actual facts.[19] A supplier could potentially have a duty to *defend* a contractor against a claim, but not have a duty to *indemnify* if the facts revealed that the claim was baseless or outside the scope of the agreement. The general remedy for breaching a contractual duty to defend is reasonable defense and settlement costs, subject to any limitations in the agreement.[20] For example, suppose an agreement sets forth that a subcontractor is obligated to defend and indemnify a GC only for the subcontractor's own negligence. The subcontractor would be liable for costs of suit and settlement, but only up to its percentage of fault.[21]

B. Prompt and Reasonable Notice

Even if a duty to defend does arguably exist, the indemnitee must give the indemnitor reasonable notice of the claim. Whether the agreement sets forth a notice requirement or not, every contract contains an implied duty of good faith and fair dealing.[22] Fairness requires prompt notice so that an indemnitor can respond to the claim and protect its interests as the party ultimately paying the bill. Failure to provide reasonable notice breaches that implied condition of the contract and forfeits the right to defense and indemnification. There is no fixed time period for what is reasonable, so whether notice is proper depends on the facts of each particular case.

C. Right to Control Defense

[16] *Fabco Equipment, Inc. v. Kreilkamp Trucking, Inc.*, 841 N.W.2d 542.
[17] *Newhouse v. Citizens Sec. Mut. Ins. Co.*, 176 Wis.2d 824, 501 N.W.2d 1 (1993).
[18] *Estate of Krielfall v. Sizzler USA Franchise, Inc.*, 342 Wis.2d 29, 816 N.W.2d 853 (2012).
[19] *Hamlin*, 86 F.3d 93 (1996).
[20] *Fabco*, 841 N.W.2d 542 (2013).
[21] *Id*.
[22] *Kreckel v. Walbridge Aldinger Co.*, 295 Wis.2d 649, 721 N.W.2d 508 (Wis. Ct. App. 2006).

Indemnity and defense agreements may also provide that the indemnitee has the right to employ attorneys of its choice, or to control the defense and settlement negotiations. Those terms are most frequently included in liability insurance policies, but they do appear in construction contracts fairly often as well. Just as in most other indemnification issues, the rights and duties of the parties primarily depend on the contract language. Where there is no contract provision to the contrary, an indemnitee has no right to choose counsel or control the defense once its tender has been accepted by the other party.[23] If there is a provision giving the indemnitee those rights, it would most likely be enforceable.

V. WORKER'S COMPENSATION

The issues surrounding indemnity clauses can be further complicated when an employee of a subcontractor or material supplier is injured. Generally, the employee's "exclusive remedy" against his or her employer is a claim for worker's compensation benefits.[24] A claim against the employer for bodily injury is therefore prohibited under ordinary circumstances. Further, the employer's maximum liability for worker's compensation benefits is limited by statute. Many indemnity provisions, though, include language like the following, which can seriously disrupt the careful balance of the statutory scheme:

> "This indemnity obligation shall not be limited by the provisions of any worker's compensation or similar act."

A. Waiver of Immunity

While employers are typically immune from liability outside of the Worker's Compensation Act, that immunity may be waived.[25] The rule of no liability over and above that imposed by the Act does not apply in the case of an express indemnification agreement.[26] Such an agreement must be "specific and express."[27] A contract provision like the example above would almost certainly pass muster. In fact, Wisconsin law does not require use of specific phrases, such as "employee" or "worker's compensation," to expose an employer to liability beyond the Act.[28] Even seemingly broad indemnity clauses have been found sufficient to waive an employer's immunity.

It should be noted, though, that application of such "waivers" appears restricted to indemnitees' claims to enforce their contracts, as opposed to employees' claims directly against their employers.[29] Additionally, an employer is not liable for the indemnitee's portion of liability unless the indemnity provision expressly provides, and the employer is liable for the portion

[23] *Williams v. Rexworks, Inc.*, 277 Wis.2d 495, 691 N.W.2d 897 (Wis. Ct. App. 2004).
[24] Wis. Stat. § 102.03(2).
[25] *Schaub v. West Bend Mut.*, 195 Wis.2d 181, 536 N.W.2d 123 (1995).
[26] *Larsen v. J.I. Case Co.*, 37 Wis.2d 516, 155 N.W.2d 666 (1968).
[27] *Mulder v. Acme-Cleveland Corp.*, 95 Wis.2d 173, 290 N.W.2d 276 (1980).
[28] *Schaub*, 536 N.W.2d 123.
[29] *See Fuesntes v. Federal Ins. Co.*, 1997 WL 104344 at *3 (Wis. Ct. App. 1997) (unpublished).

attributable to its own acts if provided for in the contract.[30] An employer may be liable for the indemnitee's attorney's fees if provided for in the contract.[31]

B. Subrogation and Reimbursement

Employers also have other statutory rights that can be affected by indemnity agreements. If an employer is obligated to pay worker's compensation as a result of an injury for which another person may be liable, the employer has the same right to make a claim or bring an action against that person for the employee's injury.[32] This is commonly known as "subrogation." The employer is also entitled to be reimbursement from a settlement or judgment that the employee recovers from the person responsible for the injury.[33]

However, an employer's ability to subrogate can be limited by contractual language. Wisconsin courts have found, for instance, that a general contractor's insurer could not recoup worker's compensation benefits from a subcontractor due to the language of an indemnity clause. The clause limited the subcontractor's liability to claims arising out of the subcontractor's negligence or improper workmanship.[34] On the other hand, an employer's waiver of subrogation in a service contract with a third party does not waive the employer's right to reimbursement from its employee under the Workers Compensation Act.[35] This is because the carrier's statutory right to reimbursement is not really a "subrogation" right, but rather a right of recovery from the employee.

VI. CONTRACT LAW

Various other contract issues may be of concern to subcontractors and material suppliers as well, namely the effects of not signing a contract or altering the contract before signing it. In a sense, the law of contracts is one of the simplest and one of the most complex areas of the law simultaneously. At its core is the process of offer and acceptance (or "mutual assent"), supported by "consideration," which is essentially the exchange of one thing for another, be it goods services, money, or promises. As commonsense as that may seem, the formation and enforcement of contracts in the real world is often far more complicated.

A. Writing and Signature Requirements

With regard to the matter of signing contracts, one might think that not signing equates to not agreeing. However, that is very often not the case, at least not in the legal sense. There are certain types of contracts that are void unless they are put into writing and signed by a party before it can be enforced against him or her. This writing requirement is known as the "statute of frauds."[36] It covers agreements that are not to be performed within one year; promises to answer for the debt, default, or miscarriage or another person; and certain agreements related to

[30] *Young v. Anaconda Am. Brass Co.*, 43 Wis.2d 36, 168 N.W.2d 112 (1969).
[31] *See Krien v. Harsco Corp.*, 745 F.3d 313 (7th Cir. 2014).
[32] Wis. Stat. § 102.29.
[33] *Id*.
[34] *Hortman v. Otis Erecting Co., Inc.*, 108 Wis.2d 456, 322 N.W.2d 482 (Wis. Ct. App. 1982).
[35] Wis. Stat. § 102.29. *Campion v. Montgomery Elevator Co.*, 172 Wis.2d 405, 493 N.W.2d 244 (Wis. Ct. App. 1992).
[36] Wis. Stat. § 241.02.

marriage.[37] Indemnification agreements do not qualify as promises to answer for the debt of another, and they do not fall within the statute of frauds.[38] In many instances, the statute of frauds will not prevent enforcement of indemnity clauses such as those discussed in this guide, even if the subcontractor or supplier has not signed the contract.

There is a modification to the statute of frauds contained in Wisconsin's Uniform Commercial Code, which provides that all contracts for the sale of goods in excess of $500 must be in writing.[39] However, that does not necessarily apply where both parties to the contract are "merchants."[40] If both parties are merchants, the contract will be enforceable if one party gives the other written confirmation of the contract within a reasonable time.[41] The recipient must give notice of any objection to the contents of the contract within ten days after it is received.[42] As such, if a contractor sends a material supplier a sales contract to confirm an oral agreement, it may be enforceable if the supplier fails to object to the terms within ten days, whether the supplier signs it or not.[43]

B. Alteration of the Contract

Where on party alters the terms of a sales agreement between merchants, such as by adding or striking out an indemnity clause, that is considered a "proposal" for addition to the contract. It becomes a part of the agreement unless, among other things, the other party's acceptance is conditional.[44] As a general rule, conditional acceptance is treated as a rejection and a counteroffer.[45] By striking out an indemnity clause and returning it to the contractor, a subcontractor or supplier is actually rejecting the proposed contract and making a counteroffer which the contractor can either accept or reject.

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[37] *Id.*
[38] *Lingelbach v. Luckenbach*, 168 Wis. 481, 170 N.W. 711 (1919).
[39] Wis. Stat. § 402.201(1).
[40] Wis. Stat. § 402.201(2); Wis. Stat. § 402.104.
[41] Wis. Stat. § 402.201(2).
[42] *Id.*
[43] *See Cargill, Inc. v. Gaard*, 84 Wis.2d 138, 267 N.W.2d 22 (1978).
[44] Wis. Stat. § 402.207; *Mid-State Contracting, Inc. v. Superior Floor Co., Inc.*, 258 Wis.2d 139, 655 N.W.2d 142 (Wis. Ct. App. 2002).
[45] *City of Whinelander v. Boldt Const. Co.*, 195 Wis.2d 87, 537 N.W.2d 149 (Wis. Ct. App. 1995).