



IS IT TIME TO SAY BYE-BYE TO *CRAWFORD* DEFENSE CLAIMS?

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As in any commercial transaction, risk-sharing and risk-transfer considerations are important issues when negotiating indemnity provisions between the parties. This is particularly important in construction contracts.

For many years, California construction attorneys have referred informally to three levels of contractual indemnity provisions as Type I, Type II and Type III, based upon the scope of indemnity that would be afforded by the indemnitor to the indemnitee pursuant to the express terms of contractual obligations. So-called Type I indemnity afforded the broadest scope of indemnity. It addressed all damages and costs arising out of the indemnitor's work, regardless of whether the indemnitee was actively or passively at fault, but indemnity would not extend to the indemnitee's sole negligence or willful misconduct. Sometimes, indemnity provisions were drafted to say simply that indemnity would be afforded to the fullest extent permissible under California law, and the industry understood generally that was a short-hand reference to Type I indemnity. Subsequent California judicial opinions declared that the Type I – II – III designations were too mechanical, so they are not used officially any more, even though the industry still understands what they mean.

The California Legislature amended Civil Code § 2782 to render so-called Type I indemnity provisions unenforceable as against public policy when they are contained in construction contracts for residential construction entered into on or after January 1, 2006. This was good news for subcontractors and suppliers, but less so for developers, general contractors and owners who had relied on strong indemnity provisions to support their risk-sharing and risk-transfer strategies.

Then along came the *Crawford* case in 2008,¹ which seemed to breathe new life into indemnity-type claims. In short, the California Supreme Court held that, when an express indemnity provision contains language which imposes an immediate obligation upon the indemnitor to defend the indemnitee upon demand, the defense obligation is triggered even if ultimately there is no finding of negligence against the indemnitor. This contractual obligation is imposed upon the subcontractor or supplier, and is separate and distinct from any insurance obligations which might exist under that party's general liability insurance.

There has been much discussion and some trial court-level litigation in the last few years as to what the Supreme Court actually intended to do when issuing the *Crawford* decision. Subsequent published opinions have not said much, except to observe that *Crawford* did not break new ground and essentially was declarative of existing law. While *Crawford* does not resolve the entire indemnity issue, it may afford some financial relief to a beleaguered developer or general contractor who cannot afford to pay the expense associated with its own defense.

¹ *Crawford v. Weathershield Manufacturing, Inc.*, 44 Cal.4th 541 (2008).

But the Legislature continues to whittle away at so-called Type I express indemnity. In October 2011, Governor Jerry Brown signed Senate Bill 474, which will apply to all construction contracts for private commercial projects entered into on or after January 1, 2013. Whereas the previous legislative revisions were limited to residential construction, they now will apply to commercial construction as well. This is significant, since much of the construction work that has been undertaken during the financial downturn has been in the commercial arena.

There are some limitations to the new restrictions. They will not apply to Owner Controlled Insurance Programs (so-called “OCIPs”). They also will not apply to so-called Type II indemnity provisions, which allow an indemnitor to cover an indemnitee’s passive fault, which typically includes a failure to discover defects attributed to someone else’s work. Nor do they apply to design professionals.

Senate Bill 474 can affect developers and general contractors by further limiting their ability to recover indemnity dollars from subcontractors and suppliers. Arguably it will force each party to assess responsibility for its own negligence. It is unclear yet what effect Senate Bill 474 will have on *Crawford* obligations, because its emphasis on each party accounting for its own negligence seems to conflict with the no-negligence rationale of *Crawford*.

The moral of this story, at least for now, is that risk-sharing and risk-transfers remain a vital consideration when negotiating construction contracts, whether residential or commercial. To what extent they can be funded pursuant to contractual indemnity provisions, and whether an immediate defense obligation will still be possible, are all part of the ongoing question. It might be too early to say bye-bye to *Crawford* defense claims. Stay tuned.

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