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California Law Alert

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CRAWFORD REDUX: Where are the Damages?

In *Crawford v. Weather Shield Mfg., Inc.* (2008) 44 Cal 4th 541, the California Supreme Court affirmed the obligation of an indemnitor (such as a subcontractor) to defend the indemnitee (such as a general contractor and/or developer) under the express indemnity clause of a contract upon request. The duty to defend under the express indemnity provision arises immediately at the time of the request, and cannot be put off until there is a finding of liability on the part of the indemnitor. The duty to defend exists even if it is ultimately adjudicated that the indemnitor was not at fault for the for the subject loss. Even so, the duty to defend only extends to the matters embraced within the indemnity. Also, the parties are free to negotiate language that limits or precludes the defense obligation, such as making the defense obligation expressly conditioned on a finding of an indemnitor's fault.

Reaction to the *Crawford* decision has been mixed, with significant number of alleged indemnitors striving to distinguish the indemnity language in the subcontract analyzed in the *Crawford* decision from the indemnity language in the contractual provisions asserted against them and asserting other grounds to avoid the impact of *Crawford*.

Such arguments received a blow in the *UDC Universal Development L.P. v. CH2M Hill* (2010) 181 Cal.App.4th 10 decision. CH2M Hill provided engineering and environmental planning services in connection with the development of a residential condominium complex. In a trial on the developer's, UDC's, cross-complaint for express indemnity, the jury found CH2M Hill not negligent. Pointing to the language of the express indemnity agreement, CH2M Hill argued that *Crawford* was distinguishable and the defense provision in its contract did not come into play absent a finding of negligence by CH2M Hill. The indemnity clause in question stated that CH2M Hill's obligation to indemnify UDC was to the extent UDC's liability arose out of a negligent act or omission by CH2M Hill and that CH2M Hill had the obligation to defend suits brought against UDC on any claim covered by the indemnity clause. The Court of Appeal ruled that the absence of a claim of negligence by the homeowners against CH2M Hill was not sufficient to distinguish *Crawford* and also that the defense clause was not specifically tied to a finding that CH2M Hill had an actual obligation to indemnify. It further rebuffed CH2M Hill's argument that the jury finding of no negligence absolved it of a duty to defend. Finally, the Court of Appeal ruled that *Crawford* was retroactive.

In short, *CH2M Hill* held that *Crawford* means what it says.

But where were UDC's *damages*?

Bramalea California, Inc. v. Reliable Interiors, Inc. (2004) 119 Cal.App. 4th 468 held that a general contractor whose defense costs were paid by its own insurer *has no damages*. Unlike personal injury claims, the collateral source rule does not apply to an indemnitee's claim for express indemnity with respect to defense costs that are paid by an insurance company. The indemnitee does not get to "double dip" and be compensated both by its own insurance company, and by the indemnitor under an express indemnity agreement.

Crawford does not overrule *Bramalea*. Although *CH2M* Hill puts a damper on those that would attempt to argue that *Crawford* is distinguishable for some reason or another, it does not overrule *Bramalea* and in fact does not even address *Bramalea*. Perhaps CH2M Hill did not raise the *Bramalea* defense of "no damages," as the subject was never discussed in the case.

Bramalea went on to observe, in dicta, that Bramalea's general liability insurer would not be entitled to subrogation, because absent a finding that the indemnitor was at fault for causing the loss, the general contractor's insurer did not have a superior equity to the indemnitor, an essential element of subrogation. The jury finding that CH2M Hill was not negligent would seemingly have precluded any subrogation claim by UDC's insurer against CH2M Hill.

California's First Appellate District has now weighed in on the New World Order in Interstate Fire & Casualty Insurance Co. v. Cleveland Wrecking Co. (2010) ____ Cal.App.4th ___, decided February 22, 2010. Based on *Bramalea*, the trial court dismissed the subrogation action by the general contractor's insurer. There, a construction worker was injured when hit by debris during Cleveland Wrecking Company's demolition operations. Both Webcor Construction, the general contractor, and Cleveland Wrecking Company contributed to the settlement of the personal injury case and obtained good faith settlement determinations. Interstate Fire & Casualty brought suit contending it was subrogated to Webcor's express indemnity claims against Cleveland Wrecking, both with respect to its settlement payment and the defense costs it paid. The First District held that Interstate Fire sufficiently alleged entitlement to subrogation. Cleveland Wrecking argued that because Webcor had no damages due to the fact that its defense and indemnity were paid by its insurer, Interstate Fire's subrogation action also failed for lack of damages. The First District rejected the argument, because subrogation only requires that the insured *would have had* a valid claim for damages had it not been compensated by its own insurer. Clearly, had Interstate Fire not paid the defense or indemnity, Webcor would have sustained damages. Second, a valid subrogation claim does not require a *prior* finding of negligence on the indemnitor. Interstate Fire had alleged that Cleveland Wrecking's negligence was a cause of the personal injury, and that suffices at the pleading stage of a subrogation action. Consistent with *Bramalea*, as between the insurer of a general contractor or other indemnitee, and a party whose negligence in fact caused the accident or loss, the element of superior equity is established.

So far, the lay of the land is clear. A party defended and/or indemnified by its own insurer has no damages for the purpose of a complaint or cross-complaint for express indemnity. The indemnitor has a complete defense to an action *by the indemnitee*. Recovery must be by way of subrogation, if at all, and proof of fault of the indemnitor supplies the element of superior equity necessary to establish a subrogation action.

But *Interstate Fire* goes one step further. It finds that the insurer may have a superior equity *even if* the indemnitor is not at fault for causing the accident. Comparing the relative positions, an indemnitor which, like Cleveland Wrecking, agreed to indemnify the other party to the underlying transaction has a liability of greater primacy than a general liability insurer that insures against loss. The parties directly involved in the transaction are better able to evaluate and control the loss. The agreement between the parties who are connected to the incident giving rise to the loss (here, Webcor and Cleveland Wrecking) creates a greater equitable responsibility for indemnification, compared to that of a general liability insurer.

Clearly, *Crawford, CH2M Hill and Bramalea* all co-exist. To the extent that the indemnitee (e.g., general contractor) is uninsured or has a deductible, it has a claim for damages. To the extent it is insured, it has no claim for damages, and the action must be one by the insurer for subrogation or not at all. Whether *Interstate Fire's* finding that superior equity exists even in the absence of indemnitor fault will gain traction remains to be seen.

One lesson learned is that the express indemnity provisions in contracts will be enforced as written, and careful drafting of those provisions can preclude the obligation of an indemnitor to defend in the absence of fault, or before a finding of fault is made by court or jury.

The construction and coverage lawyers at Burnham Brown are here to consult and advise.

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