

**SUPPLEMENT NO. 3 TO THE REPORT OF THE LEGAL
OPINIONS COMMITTEE REGARDING LEGAL OPINIONS
IN BUSINESS TRANSACTIONS:**

**STATEMENT ON LEGAL OPINIONS REGARDING
INDEMNIFICATION AND EXCULPATION PROVISIONS
UNDER TEXAS LAW**

Legal Opinions Committee of the Business Law Section of the State Bar of
Texas

March 14, 2006

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In 1992, the Legal Opinions Committee of the Business Law Section of the State Bar of Texas (the “Committee”) published its report on legal opinions.¹ In the *Texas Legal Opinion Report*, the Committee expressly noted that enforceability issues may arise under Texas law as to transaction documents containing indemnification or exculpation provisions.² As part of its continuing effort to clarify Texas legal opinion practice, the Committee is issuing this Statement regarding Texas law enforceability opinions as to contractual provisions that purport to require indemnification of an indemnitee for, or exculpate an indemnitee from, liability for various matters, including the indemnification of an indemnitee for such indemnitee’s own acts or omissions.³ This Statement reflects the views of the Committee as of March 14, 2006 and is

¹ Legal Opinions Committee of the Business Law Section of the State Bar of Texas, *Report of the Legal Opinions Committee Regarding Legal Opinions in Business Transactions*, BULLETIN OF THE BUSINESS LAW SECTION OF THE STATE BAR OF TEXAS, Vol. 29, Nos. 2 and 3 (June-September 1992) [hereinafter *Texas Legal Opinion Report*]. The Texas Legal Opinion Report has been supplemented on two occasions. Legal Opinions Committee of the Business Law Section of the State Bar of Texas, *Supplement No. 1 to the Report of the Legal Opinions Committee Regarding Legal Opinions in Business Transactions*, BULLETIN OF THE BUSINESS LAW SECTION OF THE STATE BAR OF TEXAS, December 1994, at 1 (addressing certain Texas usury law issues); Legal Opinions Committee of the Business Law Section of the State Bar of Texas, *Supplement No. 2 to the Report of the Legal Opinions Committee Regarding Legal Opinions in Business Transactions*, BULLETIN OF THE BUSINESS LAW SECTION OF THE STATE BAR OF TEXAS, Spring 2001, at 1 (addressing Texas legal opinions regarding security interests in investment property collateral). The Texas Legal Opinion Report and both of the Supplements are available electronically at the website of the Business Law Section of the State Bar of Texas at <http://www.texasbusinesslaw.org/index.html>. This Statement was prepared by Stephen C. Tarry, Chair of the Subcommittee on Legal Opinions Regarding Indemnities, and other members of the Subcommittee, Paul H. Amiel, David R. Keyes, Gail Merel, and Richard A. Tulli, and was approved by the Committee on March 14, 2006. The Subcommittee gratefully acknowledges the assistance of J. Clark Martin in preparing and providing certain research materials that were used in the preparation of this Statement.

² *Texas Legal Opinion Report*, *supra* note 1, at 78.

³ In this Statement, for the sake of convenience, (a) references to “indemnification provisions” also include “hold harmless” provisions, (b) references to “exculpation provisions” also include release provisions and provisions that exempt a party from liability, (c) the party whose acts and omissions are indemnified by or exculpated from liability

based on Texas law and opinion practice as of such date.⁴ This Statement does not necessarily reflect the views of any particular Committee member or law firm, nor does it necessarily represent the views of the State Bar of Texas. This Statement has not been approved by the State Bar of Texas, and this Statement does not define or establish ethical or liability standards and is not intended to be given effect in any disciplinary or liability proceedings.

In reviewing this Statement, the reader should be aware that attorneys rendering opinions as to certain particular types of transactions may have developed specific opinion practices with respect to indemnification and exculpation provisions.⁵ By issuing this Statement, the Committee does not intend to imply that such opinion practices in the context of particular types of transactions are inappropriate or unacceptable.

As noted above, the purpose of this Statement is to clarify Texas legal opinion practice as it relates to enforceability opinions on contractual indemnification and exculpation provisions. To provide some legal context for the Committee's findings, this Statement begins in Part I. with a summary of existing Texas law governing the enforceability of contractual indemnification and exculpation provisions. Those readers interested in a more detailed discussion of the law (including citations to cases and other authorities) should refer to Annex 1 to this Statement. Part II. of this Statement discusses the Committee's findings on Texas legal opinion practice. Finally, Annex 2 to this Statement provides a summary of discussions in certain other legal opinion reports on remedies opinions as they relate to indemnification and exculpation provisions.

I. SUMMARY OF TEXAS LAW REGARDING INDEMNIFICATION AND EXCULPATION PROVISIONS⁶

The Texas courts have long held that parties have the right to contract as they see fit so long as their agreements do not violate the law or public policy. Texas case law does, however, impose restrictions on the ability of the parties to enter into certain contractual indemnification and exculpation provisions.

by contractual provisions is referred to as the “indemnitee,” and (d) the party who provides such an indemnity or exculpation is referred to as the “indemnitor.”

⁴ Where the Committee has not reached a conclusion as to existing customary opinion practice, this Statement sets forth the Committee's views of an acceptable opinion practice.

⁵ See, e.g., DONALD W. GLAZER, SCOTT FITZGIBBON & STEVEN O. WEISE, GLAZER AND FITZGIBBON ON LEGAL OPINIONS § 9.14.2 at 215–18 (2d ed. Cum. Supp. 2006) [hereinafter GLAZER AND FITZGIBBON] (discussing opinions regarding indemnification clauses in underwriting agreements relating to the sale of securities and indicating that the trend is to limit legal opinions on underwriting agreements to opinions that such agreements have been duly authorized, executed and delivered).

⁶ For a more detailed discussion, see *infra* Annex 1.

A. Extraordinary Shifting of Risk**1. *Negligence, Strict Statutory and Strict Products Liability*****a. *The Fair Notice Requirements: The Express Negligence Doctrine and the Conspicuousness Requirement*⁷**

Many contracts contain provisions that purport to require indemnification of an indemnitee for, or to exculpate an indemnitee from, liability for its own acts or omissions, even if such acts or omissions would constitute negligence under applicable law. Under Texas law, the fair notice requirements—which include the express negligence doctrine and the conspicuousness requirement—apply to indemnification and exculpation provisions that indemnify an indemnitee for or exculpate an indemnitee from the consequences of its own negligence or that otherwise operate to shift risk in an extraordinary way. Under the express negligence doctrine, the parties seeking to indemnify or exculpate an indemnitee for such consequences must express that intent in specific terms and within the four corners of a contract. Under the conspicuousness requirement, something (such as all capital letters or bolded or underlined text) must appear on the face of a contract to attract the attention of a reasonable person to the relevant language when he or she looks at the contract. The Texas courts have also held that both the express negligence and the conspicuousness requirements are questions of law for determination by the court.

b. *The Fair Notice Requirements: The Actual Notice or Knowledge Exception*⁸

The Texas courts have held that the fair notice requirements are not applicable when the indemnitee establishes that the indemnitor possessed actual notice or knowledge of the indemnification or exculpation provision and have also held that such actual notice or knowledge is both a question of fact and an affirmative defense with respect to which the indemnitee has the burden of proof. Most of the case law has analyzed this actual notice or knowledge exception in the context of the conspicuousness element of the fair notice requirements, and the courts have held that a variety of facts (including testimony from the signatory to a contract stating that the signatory was aware of the indemnification and exculpation provisions) are sufficient to establish such actual notice or knowledge. However, as a practical matter, it is much more difficult for an indemnitee to rely on the actual notice or knowledge exception to establish the express negligence element of the requirements—if such a provision does not by its terms expressly cover the indemnitee's own negligence, then how is the indemnitee to establish that the indemnitor had actual notice or knowledge that the provision was intended to cover such negligence? Moreover, the parol evidence rule may also present an insuperable problem for such an indemnitee to attempt to meet the express

⁷ See detailed discussion *infra* Annex 1 Part I.A.3.

⁸ See detailed discussion *infra* Annex 1 Part I.A.4.

negligence element of the requirements by introducing extrinsic evidence of intent to cover negligence.

c. The Fair Notice Requirements: Not Applicable to Past Acts⁹

The Texas courts have held that the fair notice requirements apply only to indemnification against future acts, and not to indemnification for past acts, even if the claims as to those past acts that give rise to indemnification and exculpation demands were filed after the relevant contract was signed.

2. Strict Statutory and Strict Products Liability¹⁰

The Texas courts have also held that the fair notice requirements apply to indemnification and exculpation provisions that cover strict liability claims, including strict statutory liability and strict products liability.

3. Public Policy: Gross Negligence or Intentional or Willful Misconduct¹¹

With respect to a provision indemnifying an indemnitee for or exculpating an indemnitee from liability for its own gross negligence or intentional or willful misconduct, it is unclear under current Texas case law whether such a provision is enforceable or is unenforceable as a violation of public policy. It is generally recognized that a contractual indemnification provision having the effect of indemnifying a person for such person's securities law violations may not be enforceable on public policy grounds.

4. Other Extraordinary Risk Shifting¹²

It is clear that the fair notice requirements apply to contractual provisions that have the effect of indemnifying an indemnitee for, or exculpating an indemnitee from, liability for its own negligence or for conduct for which an indemnitee would otherwise be strictly liable in tort or under applicable statutes (such as certain types of product liability). Based on the reasoning in the case law, it also appears that the fair notice requirements should apply to any such contractual provisions covering gross negligence or intentional or willful misconduct to the extent that indemnification and exculpation provisions covering gross negligence or intentional or willful misconduct are permissible under Texas law. Moreover, as is noted above, Texas courts have indicated that the fair notice requirements apply as well to indemnification and exculpation provisions that otherwise operate to shift risk in an extraordinary way.

⁹ See detailed discussion *infra* Annex 1 Part I.A.5.

¹⁰ See detailed discussion *infra* Annex 1 Part I.B.

¹¹ See detailed discussion *infra* Annex 1 Part I.C.

¹² See detailed discussion *infra* Annex 1 Part I.D.

Nevertheless, the Texas courts have also held that the fair notice requirements do not apply to contractual provisions that have the effect of allocating, as between the parties to the contract, liability for economic damages for breach of contract.

With respect to risk-shifting provisions that do not fit neatly into the categories of negligence, gross negligence, intentional or willful misconduct, strict liability or economic damages for breach of contract, what constitutes “extraordinary risk-shifting,” to which the fair notice requirements are applicable has not yet been clarified by the Texas courts.

B. Distinction Between Indemnification and Release Provisions¹³

A few Texas courts have concluded that, despite holdings to the contrary by the Texas Supreme Court, a distinction should be drawn between release provisions and indemnification provisions and that, while release provisions extinguish claims between parties to a contract, indemnification provisions only obligate an indemnitor to protect an indemnitee against third party claims. These few cases hold that in order to cover claims between the parties themselves, a contractual provision must use words indicative of an actual release—such as the words “release,” “discharge” or “relinquish.” To the extent that the holdings in these cases remain effective, broad contractual indemnification provisions that can be read to cover claims made by an indemnitor against an indemnitee could be held unenforceable by certain Texas courts if words indicative of “release” are absent. Nevertheless, the Committee believes that an opinion giver is entitled to rely on holdings of the Texas Supreme Court in rendering an opinion as to such matters.

C. Strict Construction of Indemnity Agreements¹⁴

The Texas courts have held that, while indemnity agreements should be construed to interpret the intent of the parties under normal rules of contract construction, after such rules have been applied, indemnity agreements will be strictly construed in favor of the indemnitor in order to prevent the indemnitor’s liability under the contract from being extended beyond the actual terms of the agreement.

D. Texas Statutes¹⁵

Although Texas has no statute of general application governing the enforceability of contractual indemnification and exculpation provisions, Texas statutes do, in some instances, establish rules affecting or imposing conditions on the enforceability of such provisions in certain specific types of contracts.

¹³ See detailed discussion *infra* Annex 1 Part II.

¹⁴ See detailed discussion *infra* Annex 1 Part III.

¹⁵ See detailed discussion *infra* Annex 1 Part IV.

E. Unequal Bargaining Power¹⁶

There is Texas case authority holding that contractual indemnification and exculpation provisions may be unenforceable if the parties to the contract have substantially unequal bargaining power and if such provisions are otherwise fundamentally unfair or unreasonable.

II. RENDERING LEGAL OPINIONS ON INDEMNIFICATION AND EXCULPATION PROVISIONS

A. Remedies Opinions in General

Legal opinions in business transactions often include a remedies opinion stating that, subject to certain stated qualifications, the transaction documents are enforceable against one or more of the parties to such documents.¹⁷ The *Texas Legal Opinion Report*, in discussing the meaning of a remedies opinion, explains that a remedies opinion expresses the opinion giver's opinion that each obligation and agreement of the client and each right and remedy conferred by the client would be given effect as set forth in the transaction documents insofar as governed by applicable laws, subject to certain specified exceptions.¹⁸ Thus, if a particular

¹⁶ See detailed discussion *infra* Annex 1 Part V.

¹⁷ See *Texas Legal Opinion Report*, *supra* note 1, at 64, Part VII.

¹⁸ *Id.* at 67. The Texas Legal Opinion Report states that this "broad view" of the scope of the remedies opinion is supported by two other well-known legal opinion commentaries: Section of Business Law, American Bar Association, *Third-Party Legal Opinion Report, Including the Legal Opinion Accord*, 47 BUS. L.W. 167, 198, § 10 (1991) [hereinafter *ABA Report*]; TriBar Opinion Committee, *Legal Opinions to Third Parties: An Easier Path*, 34 BUS. L.W. 1891 (1979) [hereinafter *1979 TriBar Report*]; TriBar Opinion Committee, *An Addendum—Legal Opinions to Third Parties: An Easier Path*, 36 BUS. L.W. 429 (1981); TriBar Opinion Committee, *Second Addendum to Legal Opinions to Third Parties: An Easier Path*, 44 BUS. L.W. 563 (1989). In 1998, the TriBar Opinion Committee adopted a new report that examined and replaced the TriBar Report and the Addenda thereto. TriBar Opinion Committee, *Third-Party Closing Opinions, A Report of The TriBar Opinion Committee*, 53 BUS. L.W. 591 (1998) [hereinafter *TriBar Report*]. While, for a number of years, the Business Law Section of the California Bar espoused the view that a remedies opinion addresses the enforceability of only the essential provisions of a contract, the California Business Law Section has recently concluded that "disagreement about the California view and the [broad] view has occupied an undue amount of time and energy, and should be discontinued" and that the liability of an opinion giver based on a breach of the duty of care is "quite unlikely" to be determined by whether the remedies opinion is interpreted to cover each and every provision of a contract or only the essential provisions; rather, the liability of any opinion giver depends upon whether the opinion giver has complied with customary practice in preparing and rendering a remedies opinion, and it appears that most opinion givers, regardless of their geographic location and adherence to one or other view regarding remedies opinions, exercise similar customary practices in preparing and rendering remedies opinions. State Bar of California Business Law Section, *Report on Third-Party Remedies Opinions* at 8–9 (September 2004). Nevertheless, the *Texas Legal Opinion Report* and the other authorities that adopt this "broad view" all agree that it is customary practice for an opinion giver to take various general qualifications to a remedies opinion (in addition to any that may be related to contractual indemnification and exculpation provisions), such as, for example, a qualification that the enforceability of the transaction documents is subject to the effect of bankruptcy, insolvency, reorganization, receivership, moratorium, or other similar laws

transaction document contains contractual provisions that require indemnification of an indemnitee for, or exculpate an indemnitee from, liability for such indemnitee's acts or omissions, a remedies opinion regarding the enforceability of that transaction document against the indemnitor would generally be construed in Texas as including an opinion that each such contractual provision is enforceable against the indemnitor except to the extent that qualifications and exceptions contained in the opinion have the effect of excluding, limiting or qualifying an opinion regarding such matters.

B. Texas Law Issues

In issuing a remedies opinion on the enforceability of contractual indemnification and exculpation provisions under Texas law,¹⁹ an opinion giver will need to consider a series of questions as follows:²⁰

- First, if the contractual provisions in issue involve future negligence, gross negligence, strict liability, or intentional or willful misconduct such that the fair notice requirements are applicable to such provisions, do such provisions satisfy the fair notice requirements (*i.e.*, both the express negligence doctrine and the conspicuousness requirement)?²¹ In this connection, it should be noted that the Texas courts have held that the fair notice requirements do not apply to contractual indemnification and exculpation provisions that relate to conduct occurring prior to the execution of the contract at issue.²²
- As to the express negligence doctrine, does the relevant risk-shifting language in the commercial contract compare favorably with provisions that have been approved by the Texas courts?
- As to compliance with the conspicuousness requirement, is the risk-shifting

affecting the rights and remedies of creditors generally. *See Texas Legal Opinion Report, supra*, at 68; GLAZER AND FITZGIBBON, *supra* note 5, at 91; ABA Report, *supra*, at 202; TriBar Report, *supra*, at 619.

¹⁹ To the extent that a contract contains indemnification or exculpation provisions or other provisions that may be unenforceable, an opinion giver who renders a remedies opinion as to such a contract may need to consider issues of severability and whether the possible unenforceability of such contractual provisions could affect some of the other opinions being rendered.

²⁰ An opinion giver may wish to consider whether it would be appropriate to revise an indemnification or exculpation provision in a transaction document to state that the provision applies only to the extent permitted under applicable law; inserting such language would ameliorate some of the problems for an opinion giver rendering a Texas law opinion. However, where Texas law does permit indemnification or exculpation if certain requirements are satisfied, merely inserting the phrase "to the extent permitted under applicable law" may not address whether such requirements have been satisfied, including, for example, the fair notice requirements. Therefore, the opinion giver may want to consider the impact of inserting this phrase on the need to retain otherwise applicable qualifications and exceptions in the opinion.

²¹ *See* detailed discussion *infra* Annex 1 Part I.A.3.

²² *See* detailed discussion *infra* Annex 1 Part I.A.5.

language underlined, in bold, in all capital letters or highlighted in some other manner that has been approved in the case law? If the risk-shifting provisions are scattered throughout the contract, is it enough to highlight all of the provisions or should such provisions be somehow segregated from the other contractual provisions? For example, if a particular risk-shifting provision is buried in the middle of a one hundred page contract, does highlighting such a provision comply with the conspicuousness requirement or should the provision be moved to either the beginning or end of the contract? If complying with the conspicuousness requirement results in the highlighting of a significant portion of a lengthy commercial contact, has the conspicuousness requirement really been satisfied or could one conclude, for example, that bolding, say, twenty-five percent of the language in a contract means that none of the bolded language is really conspicuous?

- If the conspicuousness requirement is not or may not be met, does the indemnitee have actual notice or knowledge of the indemnification or exculpation provision such that the conspicuousness requirement is inapplicable?²³
- Second, if the contractual provisions in issue do not involve future negligence, gross negligence, intentional or willful misconduct or strict liability, do they otherwise constitute an “extraordinary shifting of risk” such that the fair notice requirements are applicable, and if the provisions do provide for extraordinary risk-shifting, do they comply with the fair notice requirements?²⁴ A typical lengthy commercial contract may contain numerous provisions that allocate various risks between the parties, and it may be a tedious and difficult process for an opinion giver to identify and categorize all of these risk-shifting provisions. It may be even more difficult to determine whether any such risk-shifting provisions constitute an “extraordinary shifting of risk,” because no Texas court has, as of this date, identified any such provisions not involving negligence, gross negligence, intentional or willful misconduct, or strict liability.
- Third, if the contractual provisions indemnify an indemnitee for, or exculpate an indemnitee from, liability for its own gross negligence or intentional misconduct, are such provisions enforceable as a matter of public policy under Texas law? As is noted in Part I.C. of Annex 1, Texas law on this subject is not very well developed.
- Fourth, to the extent that the transaction documents contain indemnification provisions that are at least arguably broad enough to cover claims between the parties,²⁵ are

²³ See detailed discussion *infra* Annex 1 Part I.A.4.

²⁴ See detailed discussion *infra* Annex 1 Part I.D.

²⁵ We note that some contractual indemnification or exculpation provisions may purport to indemnify an indemnitee for, or exempt an indemnitee from, all or substantially all liability for damages in the event that the indemnitee breaches the contract. The Texas courts apparently have never addressed the validity of a contractual provision that completely exonerates a party, in advance, from any liability for damages upon breach and have never decided whether such a provision might constitute extraordinary shifting of risk such that the fair notice requirements

such provisions enforceable under Texas law?²⁶

- Fifth, do such contractual provisions present problems under any statutes?²⁷
- Sixth, do the parties have substantially unequal bargaining power such that the provisions would be declared void under Texas case law if the resulting provisions at issue are found to be fundamentally unfair or unreasonable?²⁸ Although, in the Committee's experience, this issue is not likely to arise in the context of a commercial contract as to which an attorney has been asked to render a legal opinion, some commercial contracts clearly do involve situations in which one party is at a significant disadvantage in the contractual negotiations.

C. Legal Opinion Qualifications

In the Committee's experience, it is customary in Texas for a remedies opinion under Texas law to include a specific qualification as to the enforceability of indemnification and exculpation provisions.²⁹ On this issue, the *Texas Legal Opinion Report* states that:

would be applicable to the provision. While there is some case authority in support of provisions contractually exonerating a party from substantial liability for breach of contract, there is also some authority suggesting that, in some circumstances, at least a fair or minimal remedy for breach of contract should be available. *See* detailed discussion *infra* Annex 1 Part I.D. and Annex 1, note 52. In such circumstances, if an opinion giver relies on qualifying language similar to that set forth at the end of the first paragraph of Part II.C.2., *infra*, the opinion giver may want to consider whether a reference to extraordinary risk-shifting should be included in such qualifying language. *See* *infra* note 35. In addition, if, at the time a legal opinion is rendered, the indemnitee that benefits from such a broad release has not given value (such as the making of a loan) or otherwise changed its position in reliance on the promises made in the contract, then the opinion giver may need to consider other legal issues that are beyond the scope of this Statement, including the more fundamental question of whether an enforceable contract exists at all. *See Texas Legal Opinion Report, supra* note 1, at 64.

²⁶ *See* detailed discussion *infra* Annex 1 Part II.

²⁷ *See* detailed discussion *infra* Annex 1 Part IV.

²⁸ *See* detailed discussion *infra* Annex 1 Part V.

²⁹ For example, in the *Texas Legal Opinion Report*, the Committee expressly approved certain common qualifications adopted in Section 14 of the *ABA Report*, including a qualification as to provisions which:

(f) limit the enforceability of provisions releasing, exculpating or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction, to the extent the action or inaction involves gross negligence, recklessness, willful misconduct or unlawful conduct

Texas Legal Opinion Report, supra note 1, at 72. *See also TriBar Report, supra* note 18, at 622 ("[I]f the opinion preparers conclude that a remedy specified in the agreement, such as an indemnification provision, is unlikely to be given legal effect, they should include an exception in the opinion"); GLAZER AND FITZGIBBON, *supra* note 5, at 140 ("opinion preparers should consider the enforceability of each undertaking of the company in the agreement, and, if they identify a provision requiring an exception, they should take it, regardless of how important they think the provision might be to the opinion recipient"). Since the indemnity qualification in the *ABA Report* excludes a

Enforceability issues also arise in transactions involving Transaction Documents containing indemnification and contribution³⁰ provisions, including securities transactions. As a result of the Second Circuit's decision in *Globus v. Law Research Serv. Inc.*³¹ that indemnification agreements in securities transactions are contrary to public policy, most lawyers add an indemnification exception in the Remedies Opinions regarding Transaction Documents containing indemnification and contribution provisions relating to actions which come within the scope of the securities laws. *Other indemnification or release provisions may not be enforceable since Texas became an express negligence state or because of laws relating to certain subjects such as drilling service contracts.*³²

Although it is customary for a remedies opinion under Texas law to include a qualification relating to indemnification and exculpation provisions, it appears that no "standard" language has developed for such a qualification; rather, Texas practitioners use a variety of different formulations.³³

remedies opinion as to indemnification and exculpation provisions involving only gross negligence, recklessness, willful misconduct or unlawful conduct, the qualification may not suffice to address Texas law issues arising from the application of the fair notice requirements to indemnification and exculpation clauses covering negligence or strict liability or otherwise providing for an extraordinary shifting of risk.

³⁰ Indemnification and contribution are distinct legal concepts. The term "contribution" is generally defined to mean a payment by each person, or by any of several persons, having a common interest or liability (such as joint tortfeasors), of his or her share of the loss suffered or money paid by one of the parties on behalf of the others. On the other hand, an indemnity involves a shift in responsibility for liability from an indemnitee to an indemnitor, usually based upon a contractual indemnification provision. *See, e.g., Lee Lewis Constr. Inc. v. Harrison*, 64 S.W.3d 1, 20 (Tex. App.—Amarillo 1999), *aff'd*, 70 S.W.3d 778 (Tex. 2001); *St. Anthony's Hosp. v. Whitfield*, 946 S.W.2d 174, 177–78 (Tex. App.—Amarillo 1997, pet. denied); 14 TEX. JUR. 3D *Contribution and Indemnification* § 1 (1997); 18 AM. JUR. 2D *Contribution* § 1 (2004). The Texas statutes expressly address contribution obligations as to tort claims. TEX. CIV. PRAC. & REM. CODE ANN. §§ 32.001, 33.002. (Vernon 2004). These statutes do not, however, purport to affect rights of indemnity. *Id.* §§ 32.001, 33.017. Thus, if a contractual provision purports to grant to an indemnitee a right of "contribution" as against an indemnitor, this right should properly be treated as an indemnity that contractually shifts risk from one party to another, even if the effect of such a provision is to alter contractually contribution rights otherwise established by statute or by common law. *See Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705, 708–09 (Tex. 1987) ("[p]arties may contract for comparative indemnity so long as they comply with the express negligence doctrine . . ."). A qualification in a legal opinion as to the enforceability of such an indemnity, therefore, should not have to address separately the legal principles related to contribution.

³¹ 418 F.2d 1276 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970).

³² *Texas Legal Opinion Report*, *supra* note 1, at 78 and n.250 (emphasis added).

³³ As will be noted upon a review of the relevant language from the various opinion reports that are summarized in Annex 2, the reports do not adopt uniform language for an opinion qualification relating to indemnification and exculpation provisions. For example, the qualifying language from the *Arizona Report* and the *Georgia Report* is somewhat similar to Section 14(f) of the *ABA Report*, *supra* note 29, but with changes reflecting the different laws of each state. On the other hand, Annex A to Appendix 10 to the *California Remedies Opinion Report* contains the following sample qualifying language: "We advise you that indemnities may be limited on statutory or public policy

1. Complete Exclusion of Indemnification and Exculpation Provisions

Part II.B. above identifies certain legal issues that may arise in rendering an opinion under Texas law on the enforceability of indemnification and exculpation provisions and states that, in order to render such an opinion, the opinion giver would have to determine both (x) whether the transaction documents contain any such provisions and also (y) whether and in what manner it would be appropriate to render an opinion on any such provisions. Based on the experience of the members of the Committee, to avoid the time and expense that is necessary for an attorney to undertake such an analysis and to craft the language for such an opinion—particularly in situations, such as certain lending transactions, where indemnification and exculpation provisions may not be that significant in the context of the overall business transaction—the parties to such transactions in Texas frequently agree that the opinion recipient will accept a legal opinion qualification that completely excludes indemnification and exculpation provisions from a Texas law enforceability opinion.³⁴ In such a situation, an opinion giver may wish to consider adopting the following legal opinion qualification that is intended to avoid all of the issues raised in Part II.B. above:

We express no opinion with respect to the validity or enforceability of the following provisions to the extent that the same are contained in the Transaction Documents: provisions purporting to release, exculpate, hold harmless, or exempt any person or entity from, or to require indemnification of or by any person or entity for, liability for any matter.

The Committee believes that, in a situation in which the parties have agreed to a complete exclusion of indemnification and exculpation provisions from a Texas law enforceability opinion, the inclusion of the qualification set forth above is an acceptable opinion practice for remedies opinions under Texas law.

The Committee notes that it is the practice of some opinion givers to disclose in the opinion letter the existence of the fair notice requirements under Texas law without rendering any opinion as to the enforceability of indemnification or exculpation provisions. An opinion giver wishing to do so might add to the qualifying language stated above a statement such as the following:

Without limiting the qualification contained in the preceding sentence, we note that,

grounds.”

³⁴ The *Texas Legal Opinion Report* and various other publications expressly recognize that costs and benefits should be considered in determining whether a legal opinion will be required on a particular issue. *Texas Legal Opinion Report*, *supra* note 1, at 43; *TriBar Report*, *supra* note 18, at 599; Committee on Legal Opinions, Section of Business Law, American Bar Association, *Guidelines for the Preparation of Closing Opinions*, 57 BUS. LAW. 875, 876 (2002); GLAZER AND FITZGIBBON, *supra* note 5, § 1.8, at 30.

in *Dresser Industries, Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505 (Tex. 1993), the Texas Supreme Court adopted certain fair notice requirements. To the extent that these requirements are applicable, parties intending to indemnify or exculpate for liability resulting from an indemnitee's negligence, gross negligence, intentional misconduct, strict statutory liability or strict products liability, or to otherwise effect extraordinary risk-shifting, must express that intent in specific terms within the text of the contract and in language that is conspicuous in the contract—*i.e.*, the specific intent must appear on the face of the contract in such a manner as would attract the attention of a reasonable person. Examples of conspicuousness given by the courts include language in capitalized headings, language in contrasting type or color, and language in an extremely short document, such as a telegram. The fair notice requirements are not applicable to the extent that the indemnitee is able to prove that the indemnitor had actual knowledge of the intended indemnification or exculpation agreement. The enforceability of indemnification and exculpation provisions in the Transaction Documents which are held not to expressly and conspicuously state this intent may be limited by the fair notice requirements described above.

2. *Other Qualifying Language*

In certain business transactions, including, for example, those in which indemnification and exculpation provisions are an important component of a transaction, the parties may determine that it is appropriate for an opinion giver to undertake a detailed review of the transaction documents to determine whether such documents contain any indemnification and exculpation provisions presenting enforceability problems under Texas law. In such situations, in which the opinion giver has agreed to render a remedies opinion regarding indemnification and exculpation provisions, the opinion giver will want to craft carefully some qualifying language that either explicitly or implicitly addresses all of the Texas law issues outlined in Part II.B. above. One example of such qualifying language is set forth below, with references to "negligence" and "extraordinary risk-shifting" in brackets to indicate that such references may be included at the option of the opinion giver, depending upon the circumstances. This language does not entirely exclude a remedies opinion as to all indemnification and exculpation provisions, but rather excludes such an opinion as to certain types of indemnification and exculpation provisions that relate to a party's own action or inaction.

Our opinion is subject to generally applicable rules of law that limit the enforceability of provisions in the Transaction Documents releasing, exculpating or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction to the extent such action or inaction involves [negligence], gross negligence, recklessness, willful misconduct or unlawful conduct [or effects any

other extraordinary risk-shifting]³⁵ or to the extent that the enforceability of such provisions is otherwise limited by public policy.

As to ordinary negligence,³⁶ if the parties to a transaction determine that it is appropriate, under the particular facts and circumstances of the transaction, for the opinion giver (and its client) to incur the time and expense necessary to consider the enforceability under Texas law of a provision indemnifying an indemnitee for, or exculpating an indemnitee from liability for, such indemnitee's own ordinary negligence, then in order for the opinion giver to render to an unqualified opinion under the logic of the *Dresser Industries, Inc.* decision and its progeny, the opinion giver would have to conclude (or take appropriate assumptions or qualifications to address) (a) that such provision satisfies the requirements of the express negligence doctrine, (b) either that (i) such provision satisfies the conspicuousness requirement or (ii) the conspicuousness requirement is inapplicable because the indemnitor possesses actual notice or knowledge of the provision, and (c) that none of the other issues discussed in Part II.B., *supra*, present problems.

An opinion letter that includes a remedies opinion as to indemnification and exculpation provisions covering ordinary negligence could be drafted in a number of different ways. One approach would be to use the sample qualifying language set forth above after the first paragraph of this Subpart2, but omit the bracketed word "negligence."

The opinion giver might also, depending upon the particular facts and circumstances, determine that it is appropriate to render a reasoned opinion that discusses the fair notice requirements and the relevant Texas judicial decisions. Although such an approach is not improper, the Committee notes that, in its experience, rendering such a reasoned opinion is not

³⁵ An opinion giver that proposes to use this qualifying language will need to decide whether to include the bracketed references to negligence and extraordinary risk-shifting. The need to include one or both of the bracketed terms will depend upon the opinion giver's analysis of the transaction documents and whether such documents contain indemnification or exculpation provisions that cover negligence or any provisions that may provide for some other extraordinary risk-shifting, possibly such as provisions that purport to indemnify or exonerate an indemnitee from all or substantially all liability for damages if the indemnitee breaches the contract. *See supra* note 25 and *infra* Annex 1 Part I.D. and Annex 1 note 91. In order better to explain the concept of extraordinary risk-shifting in the context of the fair notice requirements, an opinion giver might also consider including the qualifying language that is at the end of Part II.C.1., *supra*. For a general discussion of extraordinary risk-shifting, *see infra* Annex 1 Part I.D., which notes that, as of the date of this Statement, the only indemnification and exculpation provisions that the Texas courts have held to constitute extraordinary risk-shifting are such provisions covering the indemnitee's own negligence, gross negligence, willful or intentional misconduct or strict statutory or strict products liability. In lieu of a general reference to extraordinary risk-shifting, an opinion giver may want to identify the specific provisions in the transaction documents that may involve extraordinary risk-shifting.

³⁶ Given the state of current Texas case law, it would be difficult for an opinion giver to render a Texas law enforceability opinion as to a provision having the effect of indemnifying an indemnitee for, or exculpating an indemnitee from, liability for such indemnitee's own gross negligence or intentional misconduct. *See infra* Annex 1 Part I. C.

a customary opinion practice for Texas law remedies opinions. If an opinion giver determines to render such a reasoned opinion, in order to address the conspicuousness component of the fair notice requirements,³⁷ the opinion giver might consider relying upon a factual certificate from the officer of the indemnitor executing the transaction documents stating that such officer possesses actual notice or knowledge of the relevant indemnification or exculpation provisions.³⁸

3. *Situations Where No Qualifying Language or Other Qualifications May Be Appropriate*

Depending upon the specifics of the transaction, an opinion giver may be able to eliminate entirely any qualification as to indemnification or exculpation provisions as, for example, in those circumstances where the transaction documents do not contain provisions that raise any of the Texas law issues addressed in this Statement.

Regardless of which path the opinion giver elects to take, the opinion giver will want to consider carefully all of the provisions of the transaction documents and make sure that, among things, there are no seemingly innocuous provisions that may in fact raise indemnification or exculpation issues. If the opinion giver agrees not to include qualifying language completely excluding an opinion as to indemnification and exculpation provisions, then the opinion may need to address any such problem provisions in appropriate qualifying language or in some other acceptable manner.

III. CONCLUSION

The *Texas Legal Opinions Report* acknowledges that “no form of opinion can be drafted which is appropriate for all Transactions.”³⁹ By discussing the Texas law qualifications referred to above, the Committee does not intend to take a position as to which of such qualifications should be used in a particular transaction, and the Committee also recognizes that some attorneys may prefer to continue using different qualifications which they conclude better suit their particular circumstances. The decision whether to include any of the qualifications discussed above will have to be made by the opinion giver after a review of the transaction documents and the other relevant facts and circumstances, as well as a consideration of any further developments in Texas case law after the date of this Statement.

³⁷ See detailed discussion *infra* Annex 1 Part I.A.4.

³⁸ Although such a certificate would appear to meet the requirements of existing case law on the conspicuousness requirement, the Committee is not aware of any opinion having been rendered solely or primarily on the basis of such a certificate.

³⁹ *Texas Legal Opinions Report*, *supra* note 1, at 5.

ANNEX 1: DETAILED DISCUSSION OF TEXAS LAW REGARDING INDEMNIFICATION AND EXCULPATION PROVISIONS

The Texas courts have long recognized that “[a]s a rule, parties have the right to contract as they see fit as long as their agreement does not violate the law or public policy.”⁴⁰ As will be discussed in the following Parts of this Annex 1, Texas law does, however, impose restrictions on the ability of parties to enter into contractual indemnification and exculpation provisions that have the effect of indemnifying an indemnitee for, or exculpating an indemnitee from, liability for its own negligence, gross negligence, willful misconduct or strict liability or that otherwise have the effect of shifting risk in an extraordinary way. Texas case law regarding the distinction between indemnity agreements, on the one hand, and release agreements, on the other, may also raise issues about the enforceability of certain indemnification provisions. In addition, Texas case law imposes certain rules which, in certain circumstances, require indemnification agreements to be strictly construed in favor of the indemnitor. Finally, contractual indemnification and exculpation provisions that are the result of unequal bargaining power may also present problems under Texas case law if such provisions are fundamentally unfair or unreasonable.

I. EXTRAORDINARY SHIFTING OF RISK

A. Negligence

Many contracts contain provisions that purport to require indemnification of an indemnitee for, or to exculpate an indemnitee from, liability for its own acts or omissions, even if such acts or omissions would otherwise constitute negligence under applicable law. In a series of decisions over the years, the Texas courts⁴¹ have considered the enforceability of such provisions.

1. *The Clear and Unequivocal Language Test*

In *Fireman's Fund Insurance Co. v. Commercial Standard Insurance Co.*,⁴² the Texas Supreme Court adopted the general rule that “a contract of indemnity will not afford protection to the indemnitee against the consequences of his own negligence unless the contract clearly expresses such an obligation in unequivocal terms.”⁴³

⁴⁰ *In re The Prudential Ins. Co. of America*, 148 S.W.3d 124, 129 (Tex. 2004) (upholding a provision in a restaurant lease in which the parties waived a trial by jury); *see also* cases cited at page 129 of *In re The Prudential Ins. Co. of America*. *Id.*

⁴¹ Unless otherwise indicated, when this Annex 1 refers to or cites decisions of the federal courts of the United States, such decisions involve the application and construction of the laws of the State of Texas.

⁴² 490 S.W.2d 818 (Tex. 1973).

⁴³ *Id.* at 822.

2. *The Express Negligence Doctrine*

In its decision in *Ethyl Corporation v. Daniel Construction Co.*,⁴⁴ the Texas Supreme Court noted that certain problems had arisen in applying the “clear and unequivocal language” test laid down in *Fireman’s Fund, supra*:

[T]he 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 those ambiguous contracts.⁴⁵

The court therefore held that the “better policy” was to reject expressly the clear and unequivocal language test, and, instead, adopt the express negligence doctrine, which holds that parties seeking to indemnify an indemnitee from the consequences of its own negligence must express that intent in specific terms within the four corners of the contract.⁴⁶ The indemnification clause at issue in the *Ethyl Corp.* case provided that a construction contractor would indemnify and hold harmless the owner of the premises against “any loss or damage to persons or property as a result of operations growing out of the performance of [the construction contract] and caused by the negligence or carelessness of Contractor, Contractor’s employees, Subcontractors, and agents or licensees.”⁴⁷ The owner argued that the indemnification provision was sufficient to include an indemnity from the contractor for the owner’s negligence. The court rejected this argument and held that the indemnification provision failed to meet the express negligence test.⁴⁸ A number of Texas Supreme Court decisions have subsequently affirmed the express negligence doctrine and gone on to examine the various indemnification provisions at issue to determine whether the requirements of the express negligence test had been satisfied.⁴⁹

⁴⁴ 725 S.W.2d 705 (Tex. 1987).

⁴⁵ *Id.* at 707–08.

⁴⁶ *Id.* at 708.

⁴⁷ *Ibid.*

⁴⁸ *Ibid.*

⁴⁹ See *Maxus Exploration Co. v. Moran Bros., Inc.*, 817 S.W. 2d 50 (Tex. 1991) (indemnification provision stated that indemnitor would indemnify indemnitee against certain claims “without limit and without regard to the cause or causes thereof or the negligence of any party or parties”; court held that language satisfied the express negligence test); *Payne & Keller, Inc. v. P.P.G. Indus., Inc.*, 793 S.W.2d 956 (Tex. 1990) (contract required indemnitor to indemnify indemnitee “irrespective of whether [indemnitee] was concurrently negligent”; court held that indemnity provision met requirements of express negligence test); *Enserch Corp. v. Parker*, 794 S.W.2d 2 (Tex. 1990) (express negligence rule was satisfied by contractual indemnity provision stating that indemnity covered certain claims “regardless of whether such claims are founded in whole or in part upon the alleged negligence of the indemnitee”); *Atlantic Richfield Co. v. Petroleum Personnel, Inc.* 768 S.W.2d 724 (Tex. 1989) (indemnity applied to “negligent act or omission of [indemnitee]”; court held language met requirements of express negligence doctrine); *Gulf Coast*

3. *The Fair Notice Requirements: The Express Negligence Doctrine and the Conspicuousness Requirement*

In *Dresser Industries, Inc. v. Page Petroleum, Inc.*,⁵⁰ the Texas Supreme Court held that because the release of an indemnitee from the consequences of its own negligence is an “extraordinary shifting of risk,” the express negligence doctrine applied “to releases as well as indemnity agreements when . . . the effect of both is to relieve a party in advance for responsibility for its own negligence.”⁵¹ The court further held that “fair notice requirements” apply to indemnities, releases and other agreements that exculpate an indemnitee from the consequences of its own negligence and that these fair notice requirements include the express negligence doctrine and the conspicuousness requirement.⁵² To satisfy the conspicuousness requirement, the court held that “something must appear on the face of the contract to attract the attention of a reasonable person when he looks at it.”⁵³ With respect to the fair notice requirements, the defendant in *Dresser Industries, Inc.* argued that these requirements were questions of fact that should have been decided by a jury. The court rejected this argument, citing Section 1.201(b)(10) of the Texas version of the Uniform Commercial Code⁵⁴ that was then in effect, which provided that “whether a term or clause is ‘conspicuous’ or not is for decision by the court.”⁵⁵ The court in *Dresser Industries, Inc.* also adopted the

Masonry, Inc. v. Owens-Illinois, Inc., 739 S.W.2d 239 (Tex. 1987) (indemnification provision that did not include reference to negligence of indemnitee did not satisfy express negligence rule); *Singleton v. Crown Cent. Petroleum Corp.*, 729 S.W.2d 690 (Tex. 1987) (contractual indemnity did not satisfy express negligence test).

⁵⁰ 853 S.W.2d 505 (Tex. 1993).

⁵¹ *Id.* at 507.

⁵² *Id.* at 508.

⁵³ *Ibid.*

⁵⁴ Section 1.201(b)(10) of the current version of the Texas UCC provides as follows:

“Conspicuous,” with reference to a term, means so written, displayed, or presented that a reasonable person against which it is to operate ought to have noticed it. Whether a term is “conspicuous” or not is a decision for the court. Conspicuous terms include the following:

(A) a heading in capitals equal to or greater in size than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same or lesser size; and

(B) language in the body of a record or display in larger type than the surrounding text, or in contrasting type, font, or color to the surrounding text of the same size, or set off from surrounding text of the same size by symbols or other marks that call attention to the language.

TEX. BUS. & COM. CODE ANN. § 1.201(b)(10) (Vernon Supp. 2004-2005).

⁵⁵ Under the holdings in *Ethyl Corp.* and *Dresser Industries, Inc.*, if the express negligence doctrine applies to a particular indemnification or exculpation provision in a contract and if a court finds that the provision is ambiguous as to whether it covers negligence, then the court may not consider parol evidence to interpret the provision; rather, under the express negligence doctrine, a finding that such a provision is ambiguous means that negligence is not expressly covered and that, accordingly, a Texas court will not, as a matter of law, enforce the provision as to negligent acts and omissions. If, on the other hand, the express negligence doctrine is inapplicable for any reason, including a situation in

conspicuousness standard from Section 1.201(b)(10) in order to determine whether the conspicuousness requirement has been satisfied.⁵⁶ In applying the fair notice requirements to the facts before it, the court held that release provisions located on the back of a work order without headings or contrasting type did not satisfy the conspicuousness requirement and that the contracts were not “so short that every term in the contracts must be considered conspicuous.”⁵⁷

which the indemnitee establishes that the indemnitor has actual knowledge or notice of the provision, parol evidence should be admissible to construe the ambiguous provision in the same manner in which such evidence is admissible under general contract law principles. Since the indemnitee’s ability to prove that the indemnitor had actual knowledge or notice of the provision may, however, be adversely affected by the parol evidence rule, it may be difficult to prevail if the indemnification or exculpation clause does not unambiguously, conspicuously and expressly cover negligence. *See* discussion *infra* Part I.A.4.

⁵⁶ 853 S.W.2d at 510.

⁵⁷ *Id.* at 511; *see also* Storage & Processors, Inc. v. Reyes, 134 S.W.3d 190 (Tex. 2004) (employer must satisfy the fair notice requirements of the express negligence doctrine and conspicuousness when it enrolls employees in a non-subscriber workers’ compensation plan); Lawrence v. CDB Services, Inc., 44 S.W.3d 544 (Tex. 2001) (clause in which employee waived negligence claims against employer satisfied both express negligence and conspicuousness requirements; clause expressly referred to negligence and was in bold face and all capital letters); Littlefield v. Schaefer, 955 S.W.2d 272 (Tex. 1997) (six-paragraph release printed in “minuscule” typeface on front of one-page release and entry form did not satisfy conspicuousness requirement). Numerous subsequent decisions of the Texas and federal courts have also expounded on the scope of the fair notice requirements adopted in *Dresser Industries, Inc.* *See, e.g.*, Quorum Health Res., L.L.C. v. Maverick County Hosp. Dist., 308 F.3d 451 (5th Cir. 2002) (indemnification provision that did not mention negligence of indemnitee did not satisfy express negligence doctrine); River Prod. Co., Inc. v. Baker Hughes Prod. Tools, Inc., 98 F.3d 857 (5th Cir. 1996) (provision on invoice that failed to draw reader’s attention to such provision did not satisfy conspicuousness requirement); Am. Indem. Lloyds v. Travelers Prop. & Cas. Co., 189 F. Supp. 2d 630 (S.D. Tex. 2002) (provision satisfied fair notice requirements because provision expressly mentioned negligence and was printed on face of contract, even though neither the provision nor its heading was printed in capital letters or in bold type); Riley v. Champion Int’l Corp., 973 F. Supp. 634 (E.D. Tex. 1997) (release provision did not satisfy conspicuousness requirement because capitalized heading referred only to an indemnity and not to release and because release was in the final sentence of a lengthy provision; release did not satisfy express negligence doctrine because release did not refer to the indemnitee’s own negligence); OXY USA, Inc. v. S.W. Energy Prod. Co., 161 S.W.3d 277 (Tex. App.—Corpus Christi 2005, pet. filed) (holding fair notice requirements did not apply to indemnity agreements that are used to shift liability for actions that have already occurred); ALCOA, Reynolds Metals Co. v. Hydrochem Indus. Serv., Inc., No. 13-02-00531-CV, 2005 Tex. App. LEXIS 2010, at *18-*25 (Tex. App.—Corpus Christi Mar. 17, 2005, pet. denied) (mem.) (holding indemnity provision satisfied express negligence requirement, but that the provision, which was in small type-written text, did not satisfy conspicuousness requirement); Tamez v. Sw. Motor Transp., Inc., 155 S.W.3d 564 (Tex. App.—San Antonio 2004, no pet.) (pre-injury release agreement releasing indemnitee from liability for its own negligence satisfied express negligence doctrine and conspicuousness requirement; release expressly included negligence and contained bolded, capitalized and underlined typeface); Banner Sign & Barricade, Inc. v. Price Constr., Inc., 94 S.W.3d 692 (Tex. App.—San Antonio 2002, pet. denied) (indemnification provision in subcontract that expressly included negligence satisfied express negligence doctrine); J.M. Krupar Constr. Co. v. Rosenberg, 95 S.W.3d 322 (Tex. App.—Houston [1st Dist.] 2002, no pet.) (indemnity clause in subcontract did not include express reference to negligence and did not satisfy express negligence doctrine); Ranger Ins. Co. v. Int’l Specialty Lines Ins. Co., 78 S.W.3d 659 (Tex. App.—Houston [1st Dist.] 2002, no pet.) (express negligence test was satisfied where heading on indemnity provisions was entitled “Responsibility for

4. The Fair Notice Requirements: The Actual Notice or Knowledge Exception

In the *Dresser Industries, Inc.* decision, the Texas Supreme Court stated that “[t]he fair notice requirements are not applicable when the indemnitee establishes that the indemnitor possessed actual notice or knowledge of the indemnity agreement.”⁵⁸ Subsequent Texas court

Loss or Damage, Indemnity, Release of Liability and Allocation of Risk” and was in slightly larger font and all bold capital letters); DDD Energy, Inc. v. Veritas DGC Land, Inc., 60 S.W.3d 880 (Tex. App.—Houston [14th Dist.] 2001, no pet.) (indemnification provision that did not mention negligence failed express negligence test); Banzhaf v. ADT Sec. Sys. Sw., Inc., 28 S.W.3d 180 (Tex. App.—Eastland 2000, pet. denied) (express negligence doctrine does not require that indemnity clause use the word “negligence,” and, where indemnity provision was in enlarged, all-capital lettering, it satisfied conspicuousness requirement); UPS Truck Leasing, Inc. v. Leaseway Transfer Pool, Inc., 27 S.W.3d 174 (Tex. App.—San Antonio 2000, no pet.) (heading to indemnity section, which consisted of the words “customer agrees,” was in upper case and bold type; conspicuousness requirement was not satisfied because the heading did not mention the indemnity and the indemnity provision was not itself capitalized or in bold type); Douglas Cablevision IV, L.P. v. Sw. Elec. Power Co., 992 S.W.2d 503 (Tex. App.—Texarkana 1999, pet. denied) (contract consisting of twenty-two numbered paragraphs was printed in the same size and type of font; holding that indemnity provision in paragraph seventeen did not meet conspicuousness requirement); Polley v. Odom, 957 S.W.2d 932 (Tex. App.—Waco 1997), *judgm’t vacated per motion of parties on settlement*, 963 S.W.2d 917 (Tex. App.—Waco 1998) (express negligence doctrine was applicable to risk of loss clause in commercial lease that released landlord in advance for liability for his own negligence; clause did not meet the requirements of the doctrine because it did not expressly include negligence); Beneficial Pers. Servs. of Tex., Inc. v. Porras, 927 S.W.2d 177 (Tex. App.—El Paso 1996), *pet. granted, judgm’t vacated w.r.m.*, 938 S.W.2d 716 (Tex. 1997) (per curiam) (exculpatory clause in employment contract did not include negligence and therefore did not satisfy express negligence doctrine); Faulk Mgmt. Servs. v. Lufkin Indus. Inc., 905 S.W.2d 476 (Tex. App.—Beaumont 1995, writ denied) (hold harmless agreement indemnifying building owner for negligence of owner met requirements of express negligence doctrine); U.S. Rentals v. Mundy Serv. Corp., 901 S.W.2d 789 (Tex. App.—Houston [14th Dist.] 1995, writ denied) (indemnity provision was the seventh of fifteen unrelated provisions on reverse side of rental contract and heading of provision did not alert renters that they were entering into an indemnification agreement; court held that indemnity did not satisfy conspicuousness requirement); Rickey v. Houston Health Club, Inc., 863 S.W.2d 148 (Tex. App.—Texarkana 1993, writ denied) (waiver and release provision in health club contract did not mention negligence and therefore did not satisfy express negligence doctrine).

⁵⁸ 853 S.W.2d at 508 n.2. In support of this proposition regarding actual notice or knowledge, the court in *Dresser Industries, Inc.* cited its prior decision in *Cate v. Dover Corp.*, 790 S.W.2d 559 (Tex. 1990), which addressed the issue of whether a disclaimer of implied warranties was conspicuous enough to satisfy the requirements of the Texas version of the Uniform Commercial Code. In *Cate*, the seller argued that even an inconspicuous disclaimer should be given effect if the buyer had actual knowledge of the disclaimer, and the court agreed:

Because the object of the conspicuousness requirement is to protect the buyer from surprise and an unknowing waiver of his or her rights, inconspicuous language is immaterial when the buyer has actual knowledge of the disclaimer. This knowledge can result from the buyer’s prior dealings with the seller, or by the seller specifically bringing the inconspicuous waiver to the buyer’s attention When the buyer is not surprised by the disclaimer, insisting on compliance with the conspicuousness requirement serves no purpose. . . . The extent of a buyer’s knowledge of a disclaimer of the implied warranty of merchantability is thus clearly relevant to a determination of its enforceability. . . . The seller has the burden of proving the buyer’s actual knowledge of the disclaimer.

Id. at 561–62. The court held that, as a matter of law, merely providing a buyer with a copy of documents containing

decisions have agreed and have also concluded that such actual notice or knowledge of the indemnitor is both a question of fact and an affirmative defense with respect to which the indemnitee has the burden of proof.⁵⁹

Most of the case law on point has analyzed the actual notice or knowledge exception in the context of the conspicuousness element of the fair notice requirements. Courts have held that each of the following sets of facts is sufficient to establish such actual notice or knowledge and avoid the application of the conspicuousness requirement: (1) evidence in the summary judgment record showing that (a) an executive vice president of the indemnitor had signed a contract amendment, (b) the amendment was less than two pages in length, (c) the risk sharing part of the contract was not buried in a long provision, but was on the first page of the amendment, and (d) the indemnity and liability clause was the sole subject of the amendment;⁶⁰ (2) testimony at trial that the contract negotiations included consideration of and changes to the indemnification and exculpation provisions, together with the acts of the signatories of the parties in making and initialing numerous changes to the printed form contract;⁶¹ (3) deposition testimony of indemnitor's vice president stating that (a) he had been negotiating and/or overseeing contracts and leases for the indemnitor for nineteen years, (b) since 1989, he had read all of the leases before signing them and knew the provisions contained in those leases, (c) although he could not specifically remember looking at the lease in issue in 1989, he probably read the lease before signing it because that was his practice and he initialed changes to the leases, and (d) he read the indemnity provision before signing the lease and was aware of that provision being in the lease;⁶² (4) stipulation of the indemnitor that the president of the indemnitor read the agreement when he signed it;⁶³ and (5) deposition testimony of the indemnitor's executive vice president stating that, prior to signing the

an inconspicuous disclaimer does not establish actual knowledge. *Id.* at 562.

⁵⁹ *McGehee v. Certainfeed Corp.*, 101 F.3d 1078, 1081 (5th Cir. 1996); *ALCOA v. Hydrochem Indus. Serv., Inc.*, No. 13-02-00531-CV, 2005 Tex. App. LEXIS 2010, at *27-*28 (Tex. App.—Corpus Christi Mar. 17, 2005, pet. filed) (mem. op); *Kan. City So. Ry. Co. v. Mo. Pac. R.R.*, No. 09-04-172 CV, 2004 Tex. App. LEXIS 11845, at *2-*5 (Tex. App.—Beaumont Dec. 30, 2004, no pet. h.); *Mo. Pac. R.R. Co. v. Lely Dev. Corp.*, 86 S.W.3d 787, 791-93 (Tex. App.—Austin 2002, pet. dism'd); *Coastal Transp. Co. v. Crown Cent. Petroleum Corp.*, 20 S.W.3d 119, 126 (Tex. App.—Houston [14th Dist.] 2000, pet. denied); *Douglas Cablevision IV, L.P. v. S.W. Elec. Power Co.*, 992 S.W.2d 503, 510 (Tex. App.—Texarkana 1999, pet. denied); *Interstate Northborough Partners v. Examination Mgmt. Serv., Inc.*, No. 14-96-00335-CV, 1998 Tex. App. LEXIS 2824, at *9-*10 (Tex. App.—Houston [14th Dist.] May 14, 1998, no pet.); *U.S. Rentals, Inc. v. Mundy Serv. Corp.*, 901 S.W.2d 789, 793 (Tex. Civ. App.—Houston [14th Dist.] 1995, writ denied).

⁶⁰ *Millennium Petrochemicals, Inc. v. Brown & Root Holdings, Inc.*, 390 F.3d 336, 345 (5th Cir. 2004).

⁶¹ *Cleere Drilling Co. v. Dominion Exploration & Prod., Inc.*, 351 F.3d 642, 647-49 (5th Cir. 2003).

⁶² *Interstate Northborough Partners v. Examination Mgmt. Serv., Inc.*, No. 14-96-00335-CV, 1998 Tex. App. LEXIS 2824, at *8-*12 (Tex. App.—Houston [14th Dist.] May 14, 1998, no pet.).

⁶³ *Coastal Transp. Co. v. Crown Cent. Petroleum Corp.*, 20 S.W.3d 119, 126-127 (Tex. App.—Houston [14th Dist.] 2000, pet. denied).

contract, he was aware of the indemnity provision.⁶⁴

It is, on the other hand, much more difficult for an indemnitee to rely on the actual notice and knowledge exception to establish that the express negligence element of the fair notice requirements does not apply to a contractual indemnification or exculpation provision that on its face does not cover ordinary negligence. For example, in *DDD Energy, Inc. v. Veritas DGC Land, Inc.*,⁶⁵ the indemnitee was seeking indemnification for its own negligence, but the court held that the contractual indemnification provision did not, by its terms, cover negligence and that, accordingly, the indemnification provision failed the express negligence test.⁶⁶ The indemnitee then contended that the express negligence doctrine was inapplicable because the indemnitor possessed actual notice or knowledge of the indemnification provision. In rejecting the indemnitee's claim, the court held that "evidence of actual notice is of no moment here" since the court had already held that the indemnity clause was not sufficient to shift the responsibility for the indemnitee's negligence.⁶⁷ The parol evidence rule⁶⁸ may also present an insuperable problem for an indemnitee who is attempting to use the actual notice and knowledge exception in order to avoid the results of the express negligence doctrine. In this connection, in *Silsbee Hosp. Inc. v. George*,⁶⁹ the Beaumont Court of Appeals upheld a trial court's ruling that, in a situation in which an exculpation provision did not meet the requirements of the express negligence doctrine, extrinsic evidence regarding the indemnitor's knowledge of intended scope of the provision was inadmissible under the parol evidence rule.⁷⁰

5. *The Fair Notice Requirements: Not Applicable to Past Acts*

The *Dresser Industries, Inc.* decision examined releases and indemnity agreements, the effect of which is "to relieve a party *in advance* for its own negligence."⁷¹ Thus, by its terms, *Dresser Industries, Inc.* did not address whether the fair notice requirements should be applied to contractual indemnification and exculpation provisions that relate to conduct occurring prior to the execution of the contract. The Texas Supreme Court subsequently stated that its holding in *Dresser Industries, Inc.* "is explicitly limited to releases and indemnity clauses in which one party exculpates itself from its own *future* negligence."⁷² Other Texas courts have addressed

⁶⁴ *Air Liquide Am. Corp. v. Crain Bros., Inc.*, 11 F. Supp. 2d 709, 711–12 (S.D. Tex. 1997).

⁶⁵ 60 S.W.3d 880 (Tex. App.—Houston [14th Dist.] 2001, no pet.).

⁶⁶ *Id.* at 884.

⁶⁷ *Id.* at 884–85.

⁶⁸ The parol evidence rule holds that terms set forth in a writing intended by the parties as a final expression of their agreement may not be contradicted by evidence of a prior or contemporaneous agreement. *See* 14 WILLIAM V. DORSANEO III ET AL., TEXAS LITIGATION GUIDE § 210.04 (2005).

⁶⁹ 163 S.W.3d 284 (Tex. App.—Beaumont 2005, pet. denied).

⁷⁰ *Id.* at 293.

⁷¹ 853 S.W.2d at 508 (emphasis added).

⁷² *Green Int'l, Inc. v. Solis*, 951 S.W.2d 384, 387 (Tex. 1997) (emphasis added).

situations in which an indemnitee was not seeking indemnification or exculpation for future acts, but rather was seeking indemnification or exculpation for past events caused or contributed to by the indemnitor. In this context, these courts held that the fair notice requirements apply only to indemnification against future acts, not past acts, even if the claims as to those past acts that give rise to indemnification or exculpation demands were filed after the relevant contract was signed.⁷³

B. Strict Statutory and Strict Products Liability

In 1986, the application of the clear and unequivocal language test was extended in *Dorchester Gas Corp. v. American Petrofina Inc.*⁷⁴ to a case of strict liability so that clear and unequivocal language was required in a contract for indemnity protecting the indemnitee from strict liability for a defective product.⁷⁵ The Texas courts have also held that the express

⁷³ *OXY USA, Inc. v. Sw. Energy Prod. Co.*, 161 S.W.3d 277, 282–84 (Tex. App.—Corpus Christi 2005, pet. filed) (holding that an indemnity covering pre-existing conduct was not subject to the fair notice requirements, even though claim giving rise to request for indemnification was filed after indemnity was signed); *Lehman v. Har-Con Corp.*, 76 S.W.3d 555, 559–62 (Tex. App.—Houston [14th Dist.] 2002, no pet.) (rejecting assertion that the fair notice requirements applied to an indemnity provision when the conduct at issue occurred before the indemnity was executed, but the claim was not filed until afterward); *Transcon. Gas Pipeline Corp. v. Texaco, Inc.*, 35 S.W.3d 658, 668–69 (Tex. App.—Houston [1st Dist.] 2000, pet. denied) (indemnity agreement, which was executed in 1988, was broadly drafted to cover past conduct, and the claims against the indemnitee that resulted in the indemnification requests were filed in the 1990s; holding that since the indemnitee was seeking indemnification for past events, the fair notice requirements were inapplicable); *Lexington Ins. Co. v. W.M. Kellogg Co.*, 976 S.W.2d 807, 808 (Tex. App.—Houston [1st Dist.] 1998, pet. denied) (holding that the fair notice requirements did not apply to a release benefiting the construction contractor for a chemical plant when the release was signed after construction was fully completed, even though the claim that was the subject of the lawsuit arose from an explosion that occurred more than two years after the completion of construction). With respect to the holdings of the Texas courts that the fair notice requirements are explicitly limited to releases and indemnity clauses in which one party exculpates itself from its own *future* negligence, a decision of the U.S. Fifth Circuit Court of Appeals found ambiguity in the use of the term “future negligence”:

“Future negligence” might refer to *future negligent conduct*, but it might also apply 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 against a claim filed *after* the indemnity was signed but arising from conduct that occurred *prior* to the signing of the indemnity.

Fina, Inc. v. Arco, 200 F.3d 266, 272 (5th Cir. 2000). In its decision in *Lehman v. Har-Con Corp.*, *supra*, the Houston Fourteenth District Court of Appeals referred in a footnote to the Fifth Circuit’s decision in *Fina, Inc. v. Arco*, *supra*, and expressly disagreed with the Fifth Circuit’s suggestion that the fair notice requirements might apply to claims that arise from conduct prior to the signing of an indemnity, but that are filed after the indemnity was signed. 76 S.W.3d at 561 n.2.

⁷⁴ 710 S.W.2d 541 (Tex. 1986).

⁷⁵ In *Dorchester*, the court found that the indemnity clause was not clear and unequivocal, and the indemnity

negligence doctrine applies to indemnities and exculpation provisions covering strict liability claims, including strict statutory liability and strict products liability.⁷⁶

C. Public Policy: Gross Negligence or Intentional or Willful Misconduct

Arguments can be made that even if indemnification and exculpation provisions covering gross negligence or willful misconduct comply with the fair notice requirements, such provisions may still be void as against public policy. In this regard, Texas case law with respect to the enforceability of indemnities for gross negligence or intentional or willful misconduct is not very well-developed. In *Smith v. Golden Triangle Raceway*,⁷⁷ a spectator standing in the “pit” area of a raceway had signed a document that was evidently intended to release the race promoter and others from liability for their own gross negligence. The court held that “a term in a release attempting to exempt one from liability or damages occasioned by gross negligence is against public policy.”⁷⁸ On the other hand, in *Valero Energy Corp. v. M. W. Kellogg Construction Co.*,⁷⁹ the court held that a contractual waiver and indemnity provision absolving a subcontractor of liability for its own gross negligence for work it performed at an oil refinery “does not offend public policy.”⁸⁰ It is also generally recognized that a contractual indemnification provision that has the effect of indemnifying a person for

language did not give indemnitor “fair notice” that it would be assuming responsibility for all damages caused by indemnitee after the sale of a refinery. 710 S.W.2d at 543–44. *See also* Eastman Kodak Co. v. Exxon Corp., 603 S.W.2d 208 (Tex. 1980) (contract did not clearly and unequivocally require indemnitor to indemnify indemnitee from losses proximately caused by indemnitee’s negligence).

⁷⁶ *E.g.*, Houston Lighting & Power Co. v. Atchison, Topeka, & Santa Fe Ry. Co., 890 S.W.2d 455, 458–59 (Tex. 1994).

⁷⁷ 708 S.W.2d 574 (Tex. App.—Beaumont 1986, no writ).

⁷⁸ *Id.* at 576.

⁷⁹ 866 S.W.2d 252 (Tex. App.—Corpus Christi 1993, writ denied).

⁸⁰ *Id.* at 258. *See also* Atlantic Richfield Co. v. Petroleum Personnel, Inc., 768 S.W.2d 724, 724 n.2 (Tex. 1989) (stating that the court did not decide “whether indemnity for one’s own gross negligence or intentional injury may be contracted for or awarded by Texas courts”); OXY USA, Inc. v. Sw. Energy Prod. Co., 161 S.W.3d 277 (Tex. App.—Corpus Christi 2005, pet. filed) (public policy does not prohibit an indemnity for intentional torts, particularly because, in the case at hand, actions that were the subject of the indemnity had already occurred when such indemnity was entered into); Newman v. Tropical Visions, 891 S.W.2d 713 (Tex. App.—San Antonio 1994, writ denied) (court did not address issue of whether a pre-injury release covering gross negligence violated public policy); Crown Central Petroleum Corp. v. Jennings, 727 S.W.2d 739 (Tex. App.—Austin 1987, no writ) (noting that the question of whether an indemnity can protect an indemnitee from the consequences of his own gross negligence was one of “first impression,” but did not reach the question because it found that the indemnity did not specifically express an obligation to indemnify the indemnitee for punitive damages resulting from the indemnitee’s sole gross negligence). In *Fairfield Ins. Co. v. Stephens Martin Paving, LP*, 381 F.3d 435 (5th Cir. 2004), the U.S. Court of Appeals for the Fifth Circuit certified to the Texas Supreme Court a question as to whether Texas public policy prohibits a liability insurance provider from indemnifying an award for punitive damages imposed on its insured because of gross negligence. As is noted in *Fairfield Ins. Co.*, the Texas courts have reached different conclusions on this issue. *Id.* at 437 nn.2–3.

such person's securities law violations may not be enforceable on public policy grounds.⁸¹

D. Other Extraordinary Risk Shifting

The Texas Supreme Court, in *Dresser Industries, Inc. v. Page Petroleum, Inc.*,⁸² stated that the fair notice requirements—the express negligence doctrine and the conspicuousness requirement—apply to indemnification and exculpation provisions that constitute an “extraordinary shifting of risk.” *Dresser Industries, Inc.* held that if contractual provisions have the effect of indemnifying an indemnitee for or exculpating an indemnitee from liability for its own negligence, then the fair notice requirements are applicable, unless the indemnitee establishes that the indemnitor possessed actual notice or knowledge of such provisions.⁸³ In that case, the Texas Supreme Court did not address any other “extraordinary shifting of risk.” It appears, however, that if indemnification and exculpation provisions covering gross negligence or intentional misconduct are permissible under Texas law,⁸⁴ then such provisions should also be subject to these two fair notice requirements since such contractual provisions amount to a more “extraordinary shifting of risk” than those provisions that cover only negligence.⁸⁵ To date, however, Texas courts have not resolved the issue of whether indemnification and exculpation provisions covering gross negligence or willful misconduct might be void as against public policy even if such provisions otherwise comply with the fair notice requirements.⁸⁶

In *Dresser Industries, Inc.*, the Texas Supreme Court was careful to note that its holding “was limited solely to those types of releases which relieve a party in advance of liability for its own negligence.”⁸⁷ Relying on this limitation of the holding in *Dresser Industries, Inc.*, the Texas Supreme Court subsequently held in *Green International Inc. v. Solis*⁸⁸ that a no-damages-for-delay clause in a construction subcontract did not “constitute the type of extraordinary risk-shifting found in *Dresser*”:

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-

⁸¹ See, e.g., *Laventhal, Krekstein, Horwath & Horwath v. Horwitch*, 637 F. 2d 672, 676 (9th Cir. 1980), cert. denied 452 U.S. 963 (1981); *Globus v. Law Research Serv., Inc.*, 418 F.2d 1276, 1287-89 (2d Cir. 1969), cert. denied, 397 U.S. 913 (1970). The Texas courts have apparently never addressed the enforceability of indemnification for Texas state securities laws violations.

⁸² 853 S.W.2d 505 (Tex. 1993).

⁸³ See discussion *supra* Part I.A.4.

⁸⁴ See *supra* Part I.C.

⁸⁵ See *Crown Central Petroleum Corp. v. Jennings*, 727 S.W.2d 739 (Tex. App.—Houston [1st Dist.] 1987, no writ).

⁸⁶ See *supra* Part I.C.

⁸⁷ 853 S.W.2d at 507.

⁸⁸ 951 S.W.2d 384, 387 (Tex. 1997).

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. *Dresser*, 853 S.W.2d 508. 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. *Id.* Here, the parties agreed that [the subcontractor] would bear the risk that the projects would not be completed on time, even if [the general contractor] caused the delay. This constitutes a very different type of risk-shifting than that found in *Dresser* . . .⁸⁹

The court's decision in *Green International Inc. v. Solis* is consistent with general contract law principles holding that contractual limitations on damages for breach of contract are generally enforceable⁹⁰ unless such limitations are the result of unequal bargaining power and are otherwise fundamentally unfair or unreasonable.⁹¹ With respect to a contractual provision that purports to indemnify or exonerate a party from all liability for damages for breach of contract, the Texas courts apparently have never addressed the issue of whether such a contractual provision constitutes extraordinary risk-shifting, so that the fair notice requirements would be applicable to the provision, or instead constitutes a permissible contractual limitation on damages. As to the enforceability of contractual provisions having the effect of exonerating a party from substantially all liability for such damages, there is some Texas case law generally

⁸⁹ *Id.* at 387. *See also* Capital Consultants Mgmt Corp. v. Redland Springs Ass'n, 2004 Tex. App. LEXIS 5727 (Tex. App.—San Antonio June 30, 2004, no pet.) (mem. op.) (because contract did not indemnify plaintiff for its own negligence, but rather indemnified plaintiff against acts of third party, express negligence doctrine did not apply).

⁹⁰ Section 1068 of CORBIN ON CONTRACTS states, in pertinent part, as follows:

[W]ith certain exceptions, the courts see no harm in express agreements limiting the damages to be recovered for breach of contract. Public policy may forbid the enforcement of penalties against a defendant; but it does not forbid the enforcement of a limitation in his favor. Parties sometimes make agreements and expressly provide that they shall not be enforceable at all, by any remedy legal or equitable. They may later regret their assumption of the risks of non-performance in this manner; but the courts let them lie on the bed they made. Where a contract provides that damages for breach shall not be recoverable beyond a specified sum, it is obvious that the risk of loss beyond that sum is being assumed by the promisee. If the law allows him to assume the whole risk, with no remedy whatever, it is obvious that it will allow him to assume a part less than the whole. If the contract provision is interpreted as fixing a maximum, rather than a liquidation of damages, the plaintiff will be given judgment for no more than the amount of injury that he proves, with the agreed maximum as the upper limit. In construction contracts there is often a provision limiting the items for which damages may be claimed in case of breach. Such a provision is valid.

11 ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS § 1068 (interim ed. 2002) (footnotes omitted). *See also* 24 RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS BY SAMUEL WILLISTON § 65.1 (4th ed. 2002) (footnotes omitted) (“[u]nder the fundamental principle of freedom of contract, the parties to a contract have a broad right to stipulate in their agreement the amount of damages recoverable in the event of a breach, and the courts will generally enforce such agreement, so long as the amount agreed upon is not unconscionable, is not determined to be an illegal penalty, and is not otherwise violative of public policy”); 28 TEX. JUR. 3D *Damages* § 36 (1996).

⁹¹ *See* discussion *infra* Part V.

upholding contractual limitations on liability for breach of contract, but there is also authority suggesting that, in some circumstances, adequate remedies for breach should be available.⁹²

Based on the court decisions set forth above, we have clear guidance that contractual provisions indemnifying an indemnitee for, or exculpating an indemnitee from, its own negligence or strict liability (and gross negligence and intentional misconduct if not otherwise unenforceable as against public policy) are subject to the fair notice requirements. On the other hand, under the logic set forth in *Green International Inc. v Solis, supra*, contractual provisions that shift economic damages resulting from a breach of contract are not the type of “extraordinary risk-shifting” to which the fair notice requirements apply. Nevertheless, with respect to contractual risk-shifting provisions that do not fit neatly into these categories, what constitutes “extraordinary risk-shifting” to which the fair notice requirements are applicable has not yet been decided by the Texas courts.

II. DISTINCTION BETWEEN INDEMNIFICATION AND RELEASE PROVISIONS

The *Dresser Industries, Inc.* court also examined another issue previously addressed in certain prior court decisions regarding indemnification and exculpation provisions. These prior court decisions had held that a distinction should be drawn between release and indemnification provisions and that, while release provisions extinguish claims between parties to a contract, indemnification provisions only obligate an indemnitor to protect an indemnitee against third party claims. This distinction has required the courts to analyze carefully whether, in the context of claims between the parties, a particular provision was a release covering claims between the parties, or an indemnity only, which did not—or both.⁹³ The

⁹² The Texas courts have upheld provisions in certain contracts that limit the damages payable by a party upon breach. *E.g.*, *Global Octanes Texas, L.P. v. BP Exploration & Oil, Inc.*, 154 F.3d 518, 521 (5th Cir. 1998) (“[u]nder Texas law contracting parties can limit their liability in damages to a specified amount . . . and it is immaterial whether a limitation of liability is a reasonable estimate of probable damages resulting from a breach”; court upheld provision in commercial contract for the sale of a gasoline additive that limited the liability of either party to \$500,000); *Arthur's Garage, Inc. v. Racial-Chubb Sec. Sys., Inc.*, 997 S.W.2d 803 (Tex. App.—Dallas 1999, no pet.) (court upheld contractual provision limiting burglar alarm company's liability to \$350); *Vallance & Co. v. De Anda*, 595 S.W.2d 587 (Tex. Civ. App.—San Antonio 1980, no writ) (court held that contractual provision limiting burglar alarm company's liability to \$147 was valid). *But see TEX. BUS. & COM. CODE ANN. § 2.719 cmt. 1* (Vernon 2002) (“it is the very essence of a sales contract that at least minimum adequate remedies be available;” “[i]f the parties intend to conclude a contract for [a] sale [of goods] within [Chapter 2 of the Texas version of the Uniform Commercial Code] they must accept the legal consequence that there be at least a fair quantum of remedy for breach of the obligations or duties outlined in the contract”); *RESTATEMENT (SECOND) OF CONTRACTS* § 356 cmt. a (1981) (“[a] term that fixes an unreasonably small amount as damages may be unenforceable as unconscionable”); *see supra* note 25, to the Statement.

⁹³ *See, e.g.*, *Derr Constr. Co. v. City of Houston*, 846 S.W.2d 854, 858 (Tex. App.—Houston [14th Dist.] 1992, no writ); *Whitson v. Goodbodys, Inc.*, 773 S.W.2d 381, 383 (Tex. App.—Dallas 1989, writ denied). In adopting this distinction in the *Derr Constr. Co.* decision, the Houston Court of Appeals relied in part upon the decision of the Waco

Dresser Indus., Inc. court noted “the difficulty often inherent in distinguishing between these two similar provisions” and stated that, in the context of the fair notice requirements, “the technical characterization of the provision is not controlling since the fair notice requirements now apply to both indemnity agreements and releases in this context.”⁹⁴ In addition, in *Ingersoll-Rand Co. v. Valero Energy Corp.*,⁹⁵ the Texas Supreme Court held that the parties to a contract are entitled to agree to provisions that indemnify for claims that are brought by a party to the contract.⁹⁶

Despite these holdings of the Texas Supreme Court in *Dresser Industries, Inc.* and *Ingersoll-Rand Co.*, a few lower courts have continued to draw a distinction between indemnity and release provisions.⁹⁷ To the extent that these holdings remain effective after *Dresser Industries, Inc.* and *Ingersoll-Rand Co.*, one could envision a situation in which a contractual indemnity might, by its expansive terms, be broad enough to cover claims made by the indemnitor against the indemnitee, but still fail to satisfy the requirement that the contractual provision use the “magic” words that these courts have found to be indicative of release provisions—“release, discharge, [or] relinquish.”⁹⁸ As is noted in Part I.B. of the Statement, notwithstanding such lower court decisions, the Committee believes that an opinion giver is entitled to rely on the holdings of the Texas Supreme Court in *Dresser Industries, Inc.* and *Ingersoll-Rand Co.* in rendering legal opinions as to such matters.

III. STRICT CONSTRUCTION OF INDEMNITY AGREEMENTS

The Texas courts have held that indemnity agreements should be construed under normal rules of contract construction.⁹⁹ Thus, in determining the intent of the parties in indemnity agreements, the general rule is that words and phrases will be given their ordinary, popular,

Court of Appeals in *Dresser Industries, Inc.* that was subsequently reversed by the Texas Supreme Court. *Dresser Indus., Inc. v. Page Petroleum, Inc.*, 821 S.W.2d 359, 362 (Tex. App.—Waco 1991), *rev'd*, 853 S.W.2d 505 (Tex. 1993).

⁹⁴ *Dresser Indus., Inc. v. Page Petroleum, Inc.*, 853 S.W.2d 505, 509 & n.3 (Tex. App.—Waco 1993, no writ).

⁹⁵ *Ingersoll-Rand Co. v. Valero Energy Corp.*, 997 S.W.2d 203 (Tex. 1999).

⁹⁶ *Id.* at 208.

⁹⁷ See *Riley v. Champion Int'l Corp.*, 973 F. Supp. 634, 649 (E.D. Tex. 1997) (indemnification provision relates only to claims by third parties whereas a release extinguishes a claim between the parties to an agreement); *Ganske v. Spence*, 129 S.W.3d 701 (Tex. App.—Waco 2004, no pet. h.) (indemnification provision did not cover claims between the parties to a contract); *Wallerstein v. Spirt*, 8 S.W.3d 774, 779–80 (Tex. App.—Austin 1999, no pet. h.) (holding that the clear and unambiguous language of a partnership agreement constituted an indemnity and not a release; court cited decision of Waco Court of Appeals in *Dresser Industries, Inc.*, but did not mention subsequent reversal by the Texas Supreme Court).

⁹⁸ See, e.g., *Wallerstein*, 8 S.W.3d at 780.

⁹⁹ See, e.g., *Gulf Ins. Co. v. Burns Motors, Inc.*, 22 S.W.3d 417, 423 (Tex. 2000); *Assoc. Indem. Corp. v. Cat Contracting, Inc.*, 964 S.W.2d 276, 284 (Tex. 1998).

and commonly accepted meanings,¹⁰⁰ and when an indemnity agreement is unambiguous, the courts “must determine the rights and liabilities by giving effect to the contract as written.”¹⁰¹ After the parties’ intent has been ascertained through ordinary rules of contract construction, the doctrine of *strictissimi juris*¹⁰²—which is a rule of substantive law and not a rule of construction—will be applied to strictly construe indemnity agreements¹⁰³ in favor of the indemnitor and to prevent the liability under the contract from being extended beyond the terms of the agreement.¹⁰⁴ The Texas Supreme Court’s ruling in *Mitchell’s Inc. v. Friedman*¹⁰⁵ describes the application of the doctrine of *strictissimi juris* as follows:

It is somewhat misleading to say that an indemnity agreement must be strictly construed in favor of the indemnitor and against the indemnitee. Although the distinction has not been frequently noted, the doctrine of *strictissimi juris* is not a rule of construction but is a principle of substantive law which is applicable after the intention of the parties has been ascertained by ordinary rules of construction. In determining the rights and liabilities of the parties, therefore, their intention will be first ascertained by rules of construction applicable to contracts generally. At this point neither party is favored over the other simply because their agreement is one of indemnity. After the intention of the parties has been determined, however, the doctrine of *strictissimi juris* applies and the liability of the indemnitor under his

¹⁰⁰ See, e.g., *Safeco Ins. Co. of America v. Gaubert*, 829 S.W.2d 274, 281 (Tex. App.—Dallas 1992, writ denied); *Aerospatiale Helicopter Corp. v. Universal Health Serv., Inc.*, 778 S.W.2d 492, 502 (Tex. App.—Dallas 1989, writ denied), *cert. denied*, 498 U.S. 854 (1990); *Keystone Equity Mgmt. v. Thoen*, 730 S.W.2d 339, 340 (Tex. App.—Dallas 1987, no writ).

¹⁰¹ *Ideal Lease Serv. v. Amoco Prod. Co.*, 662 S.W.2d 951, 953 (Tex. 1983); *Safeco Ins. Co. of America*, 829 S.W.2d at 281.

¹⁰² The Latin term “*strictissimi juris*” has been defined to mean “[o]f the strictest right or law; to be interpreted in the strictest manner.” BLACK’S LAW DICTIONARY 1463 (8th ed. 2004).

¹⁰³ The rule regarding strict construction of indemnity agreements has not been expressly applied to releases and other exculpatory agreements. In its decision in *Dresser Industries, Inc. v. Page Petroleum, Inc.*, however, the Texas Supreme Court held that the technical distinction between indemnities and releases was not controlling for the purposes of the fair notice requirements. 851 S.W.2d at 509 & n.3; *see supra* Part II. Based on the reasoning of the *Dresser Industries, Inc.* decision, it is possible that the strict rule regarding strict construction of indemnity agreements might be applicable to releases and other exculpatory agreements.

¹⁰⁴ *Ohio Oil Co. v. Smith*, 365 S.W.2d 621, 627 (Tex. 1963), *overruled on other grounds by Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705 (Tex. 1987); *Mitchell’s Inc. v. Friedman*, 303 S.W.2d 775, 777–78 (Tex. 1957), *overruled on other grounds by Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705 (Tex. 1987); *Safeco Ins. Co. of America*, 829 S.W.2d at 281; *Aerospatiale Helicopter Corp. v. Universal Health Serv., Inc.*, 778 S.W.2d 492, 502 (Tex. App.—Dallas 1989, writ denied), *cert. denied*, 498 U.S. 854 (1990); *Keystone Equity Mgmt.*, 730 S.W.2d at 340.

¹⁰⁵ 303 S.W.2d 775 (Tex. 1957), *overruled on other grounds by Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705 (Tex. 1987).

contract as thus interpreted will not be extended beyond the terms of the agreement.¹⁰⁶

IV. TEXAS STATUTES

Unlike some other states,¹⁰⁷ Texas has no statute of general application governing the enforceability of contractual indemnification and exculpation provisions. While it is beyond the scope of the Statement to consider all of the statutory provisions affecting the enforceability of indemnification and exculpation provisions, it should be recognized that Texas statutes do, in some instances, establish rules affecting the validity of such provisions in certain specific types of contracts,¹⁰⁸ such as: (a) a provision limiting the enforceability of certain indemnities pertaining to wells for oil, gas or water or to a mine for minerals,¹⁰⁹ and (b) a statute limiting the enforceability of certain indemnities relating to construction contracts.¹¹⁰ In addition, a few other Texas statutes expressly authorize or require contractual indemnification and exculpation provisions, but they also have the effect of imposing conditions on the enforceability of such provisions.¹¹¹

¹⁰⁶ *Id.* at 777–78.

¹⁰⁷ For example, California has a statute which provides that all contracts that exempt anyone from responsibility for his own fraud, willful injury to the person or property of another, or violation of law, whether willful or negligent, are against public policy. CAL. CIV. CODE § 1668 (West 1985).

¹⁰⁸ For an a discussion of Texas statutes relating to indemnities, *see generally* John J. Smither, *A Primer on Indemnity*, THE HOUSTON LAWYER, March-April 2004, at 26.

¹⁰⁹ TEX. CIV. PRAC. & REM. CODE ANN. § 127 (Vernon 2005).

¹¹⁰ TEX. CIV. PRAC. & REM. CODE ANN. § 130 (Vernon 2005).

¹¹¹ TEX. CIV. PRAC. & REM. CODE ANN. § 82 (Vernon 2005) (requiring a manufacturer of products to indemnify a seller of the products for product liability claims under certain circumstances); TEX. REV. CIV. STAT. ANN. art. 6132a-1, § 11.01 *et seq.* (Vernon 2003 & Supp. 2006) (provisions of Texas Revised Limited Partnership Act addressing indemnification of general partner); TEX. BUS. CORP. ACT ANN. art. 2.02-1 (Vernon 2003 & Supp. 2006) (addressing power of corporation to indemnify directors); TEX. REV. CIV. STAT. ANN. art. 1528n, art. 2.20 (Vernon 2006) (addressing power of limited liability company to indemnify members, managers, officers and other persons); TEX. BUS. ORGS. CODE ANN. § 8 (Vernon Supp. 2006) (addressing indemnification of directors and other agents of a corporation and the general partners and other agents of a limited partnership); TEX. BUS. ORGS. CODE ANN. § 101.402 (Vernon 2006) (addressing indemnification of members, managers and officers of a limited liability company). *See also* TEX. BUS. & COM. CODE ANN. § 2.316 (Vernon 2005) (addressing exclusion or modification of warranties in contracts for the sale of goods). For an example of a federal statute that addresses contractual indemnification provisions, *see* 42 U.S.C. § 9607(e) (2001) (provision of Comprehensive Environmental Response Compensation and Liability Act; stating that no indemnification, hold harmless or similar provision or conveyance shall be effective to transfer from the owner or operator of any vessel or facility or from any person who may be liable for a release or threat of release under such section, to any other person the liability imposed by such section, provided that “[n]othing in this subsection shall bar any agreement to insure, hold harmless or indemnify a party to such agreement for any liability under this section”).

V. UNEQUAL BARGAINING POWER

The Texas courts have held that contractual indemnification and exculpation provisions may be unenforceable if the parties to the contract have substantially unequal bargaining power. For example, in *Crowell v. Housing Authority*,¹¹² the plaintiff's father allegedly died as a result of carbon monoxide poisoning caused by a defective gas heater in an apartment leased by him from the defendant landlord. In analyzing a provision in the lease that contained a broad exculpation clause in favor of the landlord, the court held that the exculpation clause was void and contrary to public policy in part because the circumstances presented a "classic example of unequal bargaining power;" the terms of the lease were dictated by the defendant and a prospective tenant had "no choice but to accept them if he and his family are to enjoy decent housing accommodations not otherwise available to them."¹¹³ On the other hand, more recent cases not involving indemnification or exculpation provisions have generally held that unequal bargaining power is not, in and of itself, sufficient to render a contractual provision unenforceable unless the provision is fundamentally unfair or unreasonable.¹¹⁴ We note that, in the Committee's experience, the issue relating to unequal bargaining power is not likely to arise in the context of a commercial contract as to which an attorney has been asked to render to a legal opinion.

ANNEX 2: SUMMARY OF DISCUSSION RELATING TO INDEMNIFICATION AND EXCULPATION PROVISIONS FROM CERTAIN LEGAL OPINION REPORTS

I. AMERICAN BAR ASSOCIATION—BUSINESS LAW SECTION OF THE AMERICAN BAR ASSOCIATION, THIRD-PARTY LEGAL OPINION REPORT, INCLUDING THE LEGAL OPINION ACCORD, 47

¹¹² 495 S.W.2d 887, 888 (Tex. 1973).

¹¹³ *Id.* at 889; *see also* Allright, Inc. v. Elledge, 515 S.W.2d 266, 268 (Tex. 1974) (clause in contract parking agreement limiting parking garage's liability to \$100 was enforceable because "there is no circumstance that would deprive [the customer] of a freedom of choice"); Valero Energy Corp. v. M. W. Kellogg Constr. Co., 866 S.W.2d 252, 257 (Tex. App.—Corpus Christi 1993, writ denied) ("if one party is so disadvantaged that it is essentially forced to agree to an exculpatory provision, that provision will be declared void"; in the case at hand, contracting parties were "sophisticated entities, replete with learned counsel and a familiarity with the oil refinery industry," so exculpatory provision did not offend public policy).

¹¹⁴ *See* Holeman v. The Nat'l Bus. Inst., Inc. 94 S.W.3d 91, 100 (Tex. App.—Houston [14th Dist.] 2002, pet. denied) ("mere inequality of bargaining power is not sufficient, standing alone, to render a contract fundamentally unfair or unreasonable"; court held that a forum selection clause in covenant not to compete was enforceable); Barnett v. Network Solutions, Inc., 38 S.W.3d 200, 204 (Tex. App.—Eastland 2001, pet. denied) ("[i]t is the unfair use of, not the mere existence of, an unequal bargaining power that undermines a contract"; holding that forum selection clause in contract, which related to the registration of certain internet domain names, was enforceable). *See also* *In re AdvancePCS Health L.P.*, 172 S.W.3d 603, 608 (Tex. 2005) (per curiam) (adhesion contracts are not automatically unconscionable; upholding arbitration clause in contract between a pharmacy benefits management company and member pharmacies).

BUS. LAW. 167 (1991) (THE “ABA REPORT”).

Section 14 of the ABA Report provides, in pertinent part, as follows:

To the extent the Law of the Opining Jurisdiction applies any of the following rules to one or more of the provisions of a contract covered by an opinion to which this Section applies, that opinion is subject to the effect of generally applicable rules of Law that:

....

(f) limit the enforceability of provisions releasing, exculpating or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction, to the extent the action or inaction involves gross negligence, recklessness, willful misconduct or unlawful conduct . . .¹¹⁵

II. ARIZONA—STATE BAR OF ARIZONA BUSINESS LAW SECTION COMMITTEE ON RENDERING LEGAL OPINIONS IN BUSINESS TRANSACTIONS, FIRST AMENDED AND RESTATED REPORT OF THE STATE BAR OF ARIZONA BUSINESS LAW SECTION COMMITTEE ON RENDERING LEGAL OPINIONS BUSINESS TRANSACTIONS (OCT. 20, 2004) (THE “ARIZONA REPORT”).¹¹⁶

Section II.B.8.d of the *Arizona Report* provides as follows:

Despite the regular inclusion of indemnification provisions in various types of transaction documents such as stock or asset sale agreements, securities underwriting and placement agreements, and investment banking engagement letters, courts have relied on precepts of public policy to limit their enforceability when the party seeking indemnification has been found liable for negligence, gross negligence, or intentional misconduct. When indemnity language does not specifically address the effect of the indemnitee’s negligence, the indemnity agreement is generally construed to permit indemnification for a loss that results in part from an indemnitee’s passive negligence, but not for a loss that results from an indemnitee’s active negligence. If the effect of the indemnitee’s negligence is addressed in the agreement, then the agreement must

¹¹⁵ *ABA Report* at 205.

¹¹⁶ *Arizona Report*, available at <http://www.myazbar.org/SecComm/Sections/BU/ModelLegalOpinion.pdf>. (website of Business Law Section of the State Bar of Arizona).

clearly and unequivocally specify the result desired by the parties.¹¹⁷ Because the indemnity agreement may be less than unequivocally clear, or because the intent of the agreement may hinge on the post-agreement conduct of a party, an opinion on an indemnity clause requires special care. Indemnity provisions are often strictly interpreted against the party purportedly entitled to such contractual indemnification. In addition, the Securities Exchange Commission is of the view that indemnification of directors, officers, and controlling persons for liability arising under the Securities Act of 1933 is against public policy as expressed in the Securities Act of 1933 and is therefore unenforceable (RegulationS-K, Item510). Accordingly, given the legal uncertainties arising from the application of public policy and/or the future actions of the party seeking indemnification, it is common practice in some types of agreements to either expressly: (a) exclude indemnification provisions from “enforceability” opinions or (b) indicate that the opinion is subject to the effect of:

generally applicable rules of law that limit the enforceability of provisions releasing, exculpating, or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction, to the extent the action or inaction involves negligence, gross negligence, recklessness, willful misconduct, or unlawful conduct, or where such provisions would violate public policy.

In some cases, however, such broad exclusions will not be possible and the indemnity language will have to be analyzed for enforceability under prevailing case law. An alternative is to re-draft the indemnity clause so that it applies “to the maximum extent permitted by law.” Such self-limiting language provides assurances to the indemnitee while limiting coverage to indemnification that would be enforceable under prevailing law, thereby eliminative the risk of an incorrect opinion.¹¹⁸

III. **CALIFORNIA—BUSINESS LAW SECTION OF THE STATE BAR OF CALIFORNIA, REPORT ON THIRD-PARTY REMEDIES OPINIONS (SEPTEMBER 2004) (THE “*CALIFORNIA REMEDIES OPINIONS REPORT*”).**¹¹⁹

Appendix 10 to the *California Remedies Opinion Report* (“*California Appendix 10*”)

¹¹⁷ See *Cunningham v. Goettl Air Conditioning, Inc.*, 980 P.2d 490 (Ariz. 1999).

¹¹⁸ *Arizona Report* at 120–21.

¹¹⁹ *California Remedies Opinion Report*, available at http://calbar.ca.gov/calbar/pdfs/sections/buslaw/opinions/2005-01_remedies-opinion.pdf. (website of the Business Law Section of the State Bar of California).

contains the Report of the Exceptions Subcommittee, which was formed to assess what exceptions to a remedies opinion, other than the bankruptcy exception and the equitable principles limitation, should, consistent with customary practice, be separately stated. In preparing its report, the Exceptions Subcommittee reviewed responses to a survey conducted by the California State Bar Opinion Task Force in 2001, and this survey identified certain provisions that one or more of the respondents considered of questionable enforceability. Annex A to *California Appendix 10* summarizes the Exceptions Subcommittee's conclusions as to certain of these survey provisions.

A. Indemnities of a Party in Respect of its own Misconduct. In the case of indemnities of a party for damages arising out of, or that purport to release or exculpate a party from its own misconduct, the Exceptions Subcommittee concluded that a remedies opinion exception is "sometimes required" and noted the following in a parenthetical:

Not all indemnities are problematic, but an exception is appropriate if the indemnity in question purports to indemnify a party in a manner that is limited by public policy, such as against its own gross negligence or willful misconduct. In certain cases—for example, with respect to regulated investment advisers—public policy prohibits indemnification against the indemnified party's own negligence.¹²⁰

Annex B to *California Appendix 10* contains a more complete discussion of the Exception Subcommittee's reasoning as to particular exceptions, and the following addresses the exception relating to indemnities of a party in respect of its own misconduct:

The 1989 Report (at ¶ V.C.1) noted the reluctance of California courts "to enforce provisions requiring one party to indemnify another party for loss or damage resulting in part from the second party's wrongful or negligent acts." While express contractual provisions indemnifying (or purporting to release or exculpate) a party for damages arising out of its own negligence or misconduct have generally been held to be enforceable under recent California law, the traditional "general rule" that a party will not be indemnified for its own active negligence under a "general" indemnity agreement has not been wholly abandoned in the most recent cases addressing this issue. The result is that while acknowledging the enforceability of express indemnification provisions, the courts subject them to strict judicial scrutiny as to the reasonable intent of the parties, in most cases strictly construe them against the party claiming contractual indemnification, and subject them to public policy and equitable principles considerations. The resulting uncertainty with respect to the enforceability of these contractual provisions in any given set of circumstances is sufficiently great

¹²⁰ *California Appendix 10*, Annex A, at A-3, 4.

that California attorneys have generally avoided rendering unqualified enforceability opinions to that effect.

Indemnity Provisions Generally: The California Supreme Court has characterized indemnity as “the obligation resting on one party to make good a loss or damage another party has incurred.” *Rossmoor Sanitation, Inc. v. Pylon, Inc.*, 13 Cal. 3d 622 (1975). Prior to *Rossmoor*, judicial interpretation of express indemnity agreements under California law generally followed the rule in *MacDonald & Kruse, Inc. v. San Jose Steel Co.*, 29 Cal. App. 3d 413 (1972) which focused on the indemnitee’s “active” or “passive” negligence when determining the enforceability of different types of indemnity agreements. The courts typically interpreted “general” indemnity provisions as granting indemnitees protection only from damages caused by their passive as opposed to active negligence. Since active negligence falls outside the scope of general indemnity and hold-harmless agreements and involves affirmative acts of malfeasance, courts would often refuse indemnification or strictly construe those agreements against the indemnitee. Thus, under this general rule, a party would not be indemnified for its own active negligence under a “general” indemnity agreement. In *Rossmoor* and subsequent cases, however, while acknowledging this general rule, the courts caution against its mechanical application, noting that the active-passive dichotomy should not be wholly dispositive of the case. In *Rossmoor*, the court held that “[w]hether an indemnity agreement covers a given case turns primarily on contractual interpretation, and it is the intent of the parties as expressed in the agreement that should control. When the parties knowingly bargain for the protection at issue, the protections should be afforded. This requires an inquiry into the circumstances of the damage or injury and the language of the contract; of necessity, each case will turn on its own facts.” 13 Cal. 3d at 633. The *Rossmoor* court thus concluded that a contract may expressly provide for indemnification against an indemnitee’s own negligence, but that such an agreement “must be clear and explicit and is strictly construed against the indemnitee.” It noted that while a clause lacking such clarity and explicitness with regard to an indemnitee’s negligence (*i.e.*, a “general” indemnity clause) may be “construed to provide indemnity for a loss resulting in part from an indemnitee’s passive negligence, [it] will not be interpreted to provide indemnity if an indemnitee has been actively negligent.” *Id.* at 627-28.

In *Morton Thiokol, Inc. v. Metal Building Alteration Co.*, 193 Cal. App. 3d 1025 (1987), the court reaffirmed and expanded upon the *Rossmoor* court’s interpretive framework, and held that indemnity agreements are valid despite the indemnitee’s active negligence and despite the agreement’s failure expressly to address this negligence (*i.e.*, in the context of “general” indemnity provisions). The court held

that “ . . . indemnity should be afforded under any circumstances where to do so furthers the manifest intent of the parties to the contract and where the loss sustained would not have occurred without the indemnitor’s negligence.” *Id.* at 1029. This doctrinal approach has been substantially reaffirmed in *Hernandez v. Badger Construction Equipment Co.*, 28 Cal. App. 4th 1791 (1994), *Rooz v. Kimmel*, 55 Cal. App. 4th 573 (1997) (noting that the general rule disallowing actively negligent party’s recovery under a general indemnity provision is only a method for ascertaining the parties’ intent), and *Heppler v. J.M. Peters Co.*, 73 Cal. App. 4th 1265 (1999) (holding that the viability of the indemnity provision is dependent on contractual interpretation, specifically the intent of the parties as expressed in the contractual agreement, that each case will depend on its own facts necessitating individual inquiry into the circumstances of the damage and the language of the contract, and that “parties to an indemnity contract have great freedom of action in allocating risk, subject to certain limitations of public policy.”).

Limitations to Indemnity Provisions: As an adjunct to traditionally strict judicial interpretation of contractual provisions indemnifying a party for damages arising out of its own misconduct and active negligence, courts have imposed additional limitations based upon public policy and equitable principles:

Construction Contracts: Responding to language in *Goldman v. Ecco-Phoenix Elec. Corp.*, 62 Cal. 2d 40, 44 (1964), the legislature in 1967 adopted Cal. Civ. Code Section 2782, which states that indemnity clauses in construction contracts may not provide indemnification for injury or loss due solely to the indemnitee’s negligence or willful misconduct, and notes that such provisions are against public policy and are unenforceable and void. This section does not prohibit indemnification when the loss or injury is due only in part to the indemnitee’s negligence or willful conduct.

Strict Liability: One line of cases has held on public policy grounds that strict products liability should be deemed a form of “active negligence” for purposes of interpreting indemnity agreements in certain circumstances. Illustrative is *Widson v. International Harvester Co.*, 153 Cal. App. 3d 45 (1984) (language imposing liability on product user must do so expressly; to hold otherwise would “thwart basic public policy behind strict liability to permit indemnification of a strictly liable defendant under a general liability clause.”). That line of cases was distinguished in *Maryland Casualty Co. v. Bailey & Sons, Inc.*, 35 Cal. App. 4th 856 (1995), which noted that those cases equated strict liability with active negligence in order specifically to avoid the anomaly of permitting a party placing a defective product into commerce to abrogate by contractual indemnification its liability to the consumer. *Id.* at 871. The

court found the public policy considerations underlying those cases to be inapplicable in a situation involving a contractor seeking indemnification from a subcontractor “who played an intricate part in the creation of the product,” rather than in the use of the product. The court determined this finding to be in furtherance of another public policy consideration; namely, “the sharing of fault among those whose conduct caused the construction defect.” *Id.* at 872.

Punitive Damages: In *Ford Motor Co. v. Home Insurance Co.*, 116 Cal. App. 3d 374 (1981), an insured sought indemnity for punitive damages against insurers as a result of defects in automobiles manufactured by the insured. The insured had argued that California Insurance Code Sections 250 and 533 allowed all liabilities, including those for punitive damages, to be insurable except losses caused by intentional acts, taking the position that strict product liability did not flow from an intentional act. The court, in holding that punitive damages are uninsurable as a matter of policy, reasoned that “the purpose of punitive damages is to punish and deter sufficiently culpable conduct . . . [and that] to accomplish this purpose, the award must be assessed against the party actually responsible for the wrong.”[sic] *Id.* at 380.

Exculpatory Provisions: California decisional law has distinguished express indemnity agreements wherein an indemnitor agrees to save the indemnitee from the legal consequences of the conduct of one of the parties or of some third person, from contractual exemptions from liability or exculpatory provisions which have as their object obtaining exemption or waiver of liability from an injured party. With regard to the latter, Cal. Cal. Civ. Code Section 1668 provides as follows:

“CERTAIN CONTRACTS UNLAWFUL. All contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent, are against the policy of the law.”

Exculpatory provisions are subject to strict judicial scrutiny and will be held invalid under Section 1668 if they “affect” or “involve” the “public interest.” *See Tunkl v. Regents of University of Cal.*, 60 Cal. 2d 92 (1963) (release from liability for future negligence imposed as a condition for admission to hospital found invalid on ground that it affected the public interest); *McCarn v. Pacific Bell Directory*, 3 Cal. App. 4th 173 (1992) (limitation of publisher’s liability to cost of advertisement does not violate public policy against releases for negligence in contracts involving the public interest).

To the extent that the provisions in question purport to exculpate a party from its own misconduct—*i.e.*, amount to a waiver of damages arising from misconduct, the proposed exception set forth in endnote 6, *supra*, adequately addresses them. Where the agreement being opined upon includes a general indemnity (*i.e.*, one that does not specifically address the indemnitee's negligence), purports to indemnify a party with respect to its own violations of law or with respect to punitive damages, or involves a transaction that is subject to statutory limitations with respect to the level of conduct that may be indemnified against and includes an indemnity provision that is not tailored to those limitations, the opinion giver may choose to include an appropriate exception. The following sample language addresses indemnity provisions in these circumstances:

We advise you that indemnities may be limited on statutory or public policy grounds.

The Subcommittee believes that, as a matter of customary usage, the reference to "statutory" grounds for limitation of an indemnity obligation should be understood to include regulatory grounds, as well.¹²¹

B. Indemnification for Securities Law Liabilities. In the case of indemnities of a party for securities law liabilities, the Exceptions Subcommittee concluded that a remedies opinion exception is "usually required" and noted that "[t]here are statutory, regulatory, common law and case law limitations on indemnities for securities law liabilities."¹²² In addition, as is noted above, Annex B to *California Appendix 10* contains a more complete discussion of the Exception Subcommittee's reasoning as to particular exceptions, and the following addresses the exception relating to indemnification for securities law liabilities:

In general, indemnification provisions are enforceable under California law. See *Wagner v. Benson*, 101 Cal. App. 3d 27, 36 (1980); Cal. Civ. Code § 2772. California's state courts have not specifically addressed whether indemnification for

¹²¹ *California Appendix 10*, Annex B, at B-26 to 28. The quoted text refers to a proposed exception in endnote 6 in Annex B to *California Appendix 10* and states that such proposed exception adequately addresses contractual provisions that "purport to exculpate a party from its own misconduct...." *Id.* at B-28. This proposed exception in endnote 6 provides as follows:

We advise you that waivers of the following may be limited on statutory or public policy grounds: (i) broadly or vaguely stated rights, (ii) benefits of statutory, regulatory or constitutional rights, (iii) unknown future defenses, or (iv) rights to damages.

Id. at B-11.

¹²² *California Appendix 10*, Annex A, at A-4.

securities law liabilities is enforceable, however, and federal law applies to indemnification provisions concerning securities liabilities arising under federal securities laws. While courts disfavor contractual provisions that impede an investor's ability to enforce his or her rights under the securities laws, there is judicial reticence to encroach upon the freedom of parties to contract. See *Stratmore v. Combs* [II], 723 F. Supp. 458, 461 (N.D.Cal. 1989) rev'd on other grounds. Moreover, an indemnification provision may not shift securities liability to another party. See, e.g., *Laventhal, Krekstein, Horwath & Horwath v. Horwitch*, 637 F. 2d 672, 676 (9th Cir. 1980) cert. denied[,], 452 U.S. 963 (1981), in which an underwriter and an accounting firm sought indemnity against the issuer in respect of misrepresentations in materials prepared for a public offering of the issuer's securities. The Laventhal court explained that allowing a party to escape liability for misrepresentations in the context of a securities transaction would thwart the goal of the federal securities laws: to encourage diligence and to deter negligence.

Section 14 of the Securities Act of 1933 (the "Act"), 15 U.S.C. §77n, voids any waiver of compliance with federal securities laws. Federal courts uniformly agree that a buyer of securities may not enforceably waive its right to enforce the securities laws, and provisions to that effect would be covered by the exception discussed in endnote 6, *supra*. A more difficult question concerns whether an indemnification provision may provide that a buyer will indemnify a seller for damages resulting from misrepresentations by the buyer in a securities purchase agreement, even though the claims in respect of which indemnity is claimed by the seller involve breaches of the securities laws (e.g., if a buyer represents to the seller that the buyer is not relying on any oral representations of the seller in connection with its purchase of securities from the seller, but later brings an action against the seller asserting fraud based on alleged oral misrepresentations, whether the buyer's indemnity of the seller in respect of misrepresentations by the buyer will permit the seller to recover attorneys' fees from the buyer, even though the buyer's underlying claim is for violation by the seller of applicable securities law). With regard to these types of indemnification provisions, courts typically align with the reasoning of one of two seminal cases. The more restrictive view was pronounced in *Doody v. E.F. Hutton & Co., Inc.*, 587 F. Supp. 829 (D.Minn. 1984), in which the court refused to enforce an indemnification provision that would have forced the buyer to pay the seller's attorneys' fees in a securities fraud action. A more liberal approach was taken by the court in *Zissu v. Bear, Stearns, & Co.*, 627 F. Supp. 687 (S.D.N.Y. 1986), where the court enforced an indemnification provision despite the buyer's argument that enforcing indemnification provisions that require a plaintiff to pay for a defendant's attorneys' fees in a securities fraud action was against the public interest.

There is little Ninth Circuit case law addressing the enforceability of these types of indemnification provisions. At least one case, however, has held that an indemnification provision may be enforced where it pertains to the warranties and representations made by buyers in a securities purchase agreement and where the contract clearly specifies the obligation of the buyer to indemnify the seller for legal fees “in the event of an unsuccessful securities law suit by [the buyer].” *Stratmore v. Combs, supra*, 723 F. Supp. at 460 (discussing the importance of *Doody*, but adopting the reasoning of *Zissu*, while applying a very strict standard of clarity with respect to the wording of the indemnity provision in question).

The public policy against permitting one party to shift liability for breaches of the securities laws to another party, the conflicting judicial policies applicable to indemnities by buyers in securities purchase transactions, and the absence of decisive relevant case law make it difficult to render an opinion regarding the enforceability of such contractual provisions. Thus, it is customary practice to include an exception in a remedies opinion relating to the enforceability of those provisions. Sample language follows:

We express no opinion regarding the enforceability of [Section __] of the [Agreement] [to the extent that it would require [the opinion giver's client] to indemnify [the opinion recipient] in respect of [the opinion recipient's] violations of securities laws].¹²³

IV. GEORGIA—CORPORATE AND BANKING LAW SECTION OF THE STATE BAR OF GEORGIA, REPORT ON LEGAL OPINIONS TO THIRD PARTIES (1992) (THE “GEORGIA REPORT”).¹²⁴

With respect to indemnities, the *Georgia Report* states that any remedies opinion that adopts the conventions of the *Georgia Report* will be deemed to include and be subject to the following implied exception:

The possible unenforceability of provisions requiring indemnification for, or providing exculpation, release, or exemption from liability for, action or inaction, to the extent such action or inaction involves negligence or willful misconduct or to the

¹²³ *California Appendix 10*, Annex B, at B-29 to 31 (footnotes omitted). The quoted text refers to a proposed exception that is discussed in endnote 6 to Annex B to *California Appendix 10*. This proposed exception is quoted in full in footnote 121 to this Annex 2.

¹²⁴ *Georgia Report*, available at <http://www.gabar.org/public/pdf/sections/buslaw/lotpct.pdf>. (website of the Business Law Section of the State Bar of Georgia).

extent otherwise contrary to public policy.¹²⁵

The *Georgia Report* also contains the following explanation of this implied exception:

It is widely recognized that indemnification agreements in business transactions may be subject to significant limitations on their enforceability because of considerations of public policy. Perhaps best known are questions regarding limitations on enforceability of such provisions in connection with violations of the federal securities laws. See Globus v. Law Research Serv., Inc., 287 F. Supp 188 (S.D.N.Y.) (an underwriter may not be indemnified by an issuer for liabilities growing out of statements in an offering circular of which the underwriter has knowledge), rev'd as to other matters, 418 F.2d 1276 (2d Cir. 1969), cert. denied, 397 U.S. 913 (1970); Laventhal, Krekstein, Horwath & Horwath v. Horwitch, 637 F.2d 672 (9th Cir. 1980) (indemnification of underwriters who prepared misleading statements in offering circular would undermine statutory purpose of Securities Act of 1933 of assuring diligent performance of duty and deterring negligence; indemnity claims properly dismissed), cert. denied, 452 U.S. 963 (1981). Public policy limits may also arise in other contexts. See, e.g., Koster v. Warren, 297 F.2d 418 (9th Cir. 1961) (antitrust); Sovereign Camp W.O.W. v. Heflin, 188 Ga. 234, 3 S.E.2d 559 (1939) (fraud); Brady v. Glosson, 87 Ga. App. 476, 74 S.E.2d 253 (1953) (willful or reckless acts amounting to intentional acts).

The Georgia cases on the enforceability of indemnity and exculpation provisions generally cite and rely upon O.C.G.A. § 13-8-2 (1982 and Supp. 1990), the Code provision which provides that contracts which contravene public policy are generally unenforceable. See, e.g., Porubiansky v. Emory University, 156 Ga. App. 602, 275 S.E.2d 163 (1980) (dentist not permitted to exculpate negligence liability to patients), aff'd 248 Ga. 391, 232 S.E.2d 903 (1981).

An extended line of cases specifically recognizes Georgia public policy limitations on an entity's ability to be indemnified against its own negligence. See United States v. Seckinger, 408 F.2d 146 (5th Cir. 1969), rev'd, 397 U.S. 203 (1970), reh'g denied, 397 U.S. 1031 (1970); McMichael v. Robinson, 162 Ga. App. 67, 290 S.E.2d 168 (1982); Brown v. Seaboard Coast Line Ry. Co., 554 F.2d 1299 (5th Cir.), reh'g denied, 559 F.2d 29 (5th Cir.), cert. denied, 434 U.S. 975 (1977); Molly Pitcher Canning Co. v. Central of Georgia Ry. Co., 149 Ga. App. 5, 253 S.E.2d 392 (1979), Southern Ry. Co. v. Brunswick Pulp & Paper Co., 376 F. Supp. 96 (S.D. Ga. 1974);

¹²⁵ *Id.* at 80-81.

Carlton v. Hoskins, 134 Ga. App. 558, 215 S.E.2d 321 (1975). In addition, O.C.G.A. § 13-8-2 (1982 and Supp. 1990) specifically prohibits such indemnification and hold harmless provisions in construction, building repair, and related contracts.

The Georgia Code also contains other specific limits on indemnification. See, e.g., O.C.G.A. § 14-2-851 (1989) (limits on corporate authority to indemnify directors); O.C.G.A. § 14-9-108 (1989) (limits on indemnification of partners). Release law in Georgia is not generally subject to peculiarities of enforcement such as those contained in California Civil Code Section 1542, although factual questions involving the intended scope of the release, particularly when such a release is anticipatory, can arise.¹²⁶

V. NEW YORK—TRIBAR OPINION COMMITTEE, THIRD-PARTY CLOSING OPINIONS, A REPORT OF THE TRIBAR OPINION COMMITTEE, 53 BUS. LAW. 592 (1998) (THE “TRIBAR REPORT”).

Section 3.2 of the *TriBar Report* provides, in pertinent part, as follows:

Customary practice requires that any limit on the remedies opinion be explicit and not by way of omission of characteristic language. If an opinion giver wishes to render a remedies opinion that does not cover every undertaking of the Company in the agreement, the opinion letter should describe with particularity the limitations the opinion giver intends to impose. For example, if the opinion preparers conclude that a remedy specified in the agreement, such as an indemnification provision, is unlikely to be given legal effect, they should include an exception in the opinion.¹²⁷

VI. TEXAS—LEGAL OPINIONS COMMITTEE OF THE BUSINESS LAW SECTION OF THE STATE BAR OF TEXAS, REPORT OF THE LEGAL OPINIONS COMMITTEE REGARDING LEGAL OPINIONS IN BUSINESS TRANSACTIONS, BULLETIN OF THE BUSINESS LAW SECTION OF THE STATE BAR OF TEXAS, VOL. 29, NOS. 2 AND 3 (JUNE-SEPTEMBER 1992) (THE “TEXAS LEGAL OPINION REPORT”).

The *Texas Legal Opinion Report* states that if the legal opinion accord set forth in the *ABA Report* (the “Accord”) is adopted in an opinion letter, then the remedies opinion and any other

¹²⁶ *Id.* at 93–94.

¹²⁷ *TriBar Report* at 622. At the end of the quoted provision, the *TriBar Report* contains a footnote citing, as an example, *Globus v. Law Research Serv., Inc.*, 418 F.2d 1276, 1287–89 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970). *Id.* at 622 n.70.

opinion to which the qualifications in the *Accord* are made specifically applicable are subject to the generally applicable rules of law contained in section 14 of the *Accord*, including subsection 14(f) of the *Accord*, which Subsection addresses indemnification and exculpation provisions and is quoted above in Part I. of this Annex 2.¹²⁸

The Texas Legal Opinion Report also contains the following statement regarding indemnification and contribution provisions:

Enforceability issues also arise in transactions involving Transaction Documents containing indemnification and contribution provisions, including securities transactions. As a result of the Second Circuit's decision in *Globus v. Law Research Serv., Inc.*¹²⁹ that indemnification agreements in securities transactions are contrary to public policy, most lawyers add an indemnification exception in Remedies Opinions regarding Transaction Documents containing indemnification and contribution provisions relating to actions which come within the scope of the securities laws. Other indemnification or release provisions may not be enforceable since Texas became an express negligence state or because of laws relating to certain subjects such as drilling service contracts.¹³⁰

VII. OTHER STATES: FLORIDA, MARYLAND, MICHIGAN, NORTH CAROLINA, PENNSYLVANIA AND WASHINGTON

Legal opinion reports in other states have also addressed qualifying language relating to indemnities: (a) under Florida law, "various types of indemnification contracts sometimes are held to be invalid on the ground that they are contrary to public policy," and "[i]n giving opinions on agreements pursuant to the Federal securities laws, it also is appropriate to exclude indemnity provisions from the scope of the enforceability opinion";¹³¹ (b) the following qualification should be assumed to apply in remedies opinions rendered under Maryland law regarding commercial and real estate loan transactions: "[w]e express no opinion on the enforceability of any provisions requiring the Borrower to indemnify the Lender or its agents, officers, or directors or of any provisions exculpating the Lender from liability for its action or inaction to the extent such indemnification or exculpation is contrary to public policy or law";¹³² (c) in the State of Michigan, regardless of whether the following qualification is stated, it is implicit in an opinion: "[l]imitations under common law on the enforceability of

¹²⁸ *Texas Legal Opinion Report* at 72.

¹²⁹ 418 F.2d 1276 (1969), cert. denied, 397 U.S. 913 (1970).

¹³⁰ *Texas Legal Opinion Report* at 78 & n.250.

¹³¹ Special Committee on Opinion Standards of the Florida Bar Business Law Section, *Report on Standards for Opinions of Florida Counsel*, 46 BUS. LAW. 1407, 1435-37 (1991).

¹³² Special Joint Committee of the Maryland State Bar Association, Inc. and the Bar Association of Baltimore City, *Special Joint Committee on Lawyers' Opinions in Commercial Transactions*, 45 BUS. LAW. 706, 795 (1990).

releases, ‘hold harmless’ provisions or indemnification provisions to the extent that the action or failure to act of a beneficiary of such clauses has been grossly negligent, reckless or willful”;¹³³ (d) since certain indemnification agreements may be held invalid as against public policy, a North Carolina law opinion may include an exception that no opinion is expressed as to “any provisions of the Agreement that purport to excuse a party for liability for its own acts”;¹³⁴ (e) under Pennsylvania law, “other clauses to be considered as to enforceability include those releasing a party prospectively from liability for its own wrongs, affording indemnification for securities law violations . . . [and] clauses . . . releasing a party from, or requiring indemnification for, liability for its own action or inaction, to the extent it involves negligence, recklessness, willful misconduct or unlawful conduct”;¹³⁵ and (f) non-accord legal opinions rendered in the State of Washington sometimes contain a qualification stating that a remedies opinion is subject to the effect of generally applicable rules of law that ‘limit the enforceability of provisions of releasing, exculpating or exempting a party from, or requiring indemnification of a party for, liability for its own action or inaction, to the extent that the action or inaction involves negligence, recklessness, willful misconduct or unlawful conduct. . . .’¹³⁶

¹³³ Ad Hoc Committee of the Business Law Section of the State Bar of Michigan on Standardized Legal Opinions in Business Transactions, *Report of the Ad Hoc Committee of the Business Law Section of the State Bar of Michigan on Standardized Legal Opinions in Business Transactions*, XIV MICH. BUS. L.J. 1, 33 (1991).

¹³⁴ Legal Opinion Committee of the Business Law Section of the North Carolina Bar Association, *Third Party Legal Opinions in Business Transactions, Second Edition*, 55, 57 (March 30, 2004), available at <http://business.ncbar.org>. (website of the Business Law Section of the North Carolina Bar Association).

¹³⁵ Corporation, Banking and Business Law Section of the Pennsylvania Bar Association, *Model Closing Opinion Letter (Annotated)*, reprinted in DONALD W. GLAZER, SCOTT FITZGIBBON, & STEVEN O. WEISE, GLAZER AND FITZGIBBON ON LEGAL OPINIONS, app. 19 at 17 (2d ed. 2001).

¹³⁶ Ad Hoc Committee on Third-Party Legal Opinions of the Business Law Section of The Washington State Bar Association, *Report on Third-Party Legal Opinion Practice in the State of Washington*, at 35 (Fall 1998), available at <http://www.wsba.org/lawyers/groups/businesslaw/businesslawpublications.htm>. (website of the Business Law Section of the Washington State Bar Association).