The effect of contractual indemnity clauses

By Emma Reilly and Lily Sher

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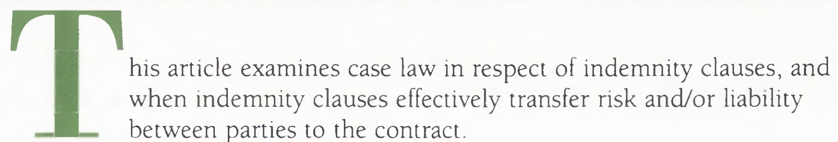
The combination of an indemnity and a requirement to be insured for the subject matter of the indemnity is a well-recognised aspect of commercial contracts. However, indemnity clauses often give rise to confusion, and litigation, as to their extent and effectiveness.



This article examines case law in respect of indemnity clauses, and when indemnity clauses effectively transfer risk and/or liability between parties to the contract.

CASE LAW – INDEMNITY CLAUSES

The leading High Court case concerning the effect of indemnity clauses is the decision in *Andar Transport Pty Limited v Brambles Limited.*[1]

Brambles Limited (Brambles) provided laundry services to a number of hospitals. Daryl Wail was employed by Brambles to deliver laundry. Brambles >>

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subsequently requested that employees such as Mr Wail create a company that could contract with Brambles in respect of the work. Mr Wail incorporated Andar Transport Pty Limited (Andar), of which he was a director, and became an employee of that entity.

On 26 July 1993, Mr Wail injured his back while he was unloading a trolley from the laundry truck. He commenced proceedings seeking damages as a result of the negligence of Brambles in respect of his injury. It was alleged that Brambles breached its duty of care by failing to ensure that the trolleys could be manoeuvred without risk of injury, having regard to their excessive weight.

Brambles joined Andar to the proceedings by way of third-party notice, seeking indemnity from Andar under the written agreement into which it had entered with Andar and, in the alternative, contribution by reference to Andar's own negligence.

Brambles relied on the following indemnity clause in the agreement:

'Clause 4.6

> *[t]o assume sole and entire responsibility for and indemnify [Brambles] against all claims liabilities losses expenses and damages arising from operation of the Vehicle by reason of any happening not attributable to the wilful negligent or malicious act or omission of [Brambles]'.*

Clause 8

8.1

Conduct the Delivery Round at its sole risk and releases [Brambles] from all claims and demands of every kind and from all liabilities of every kind which may arise in respect of any accident loss or damage to property or death of or injury to any person of any nature or kind in the conduct of the Delivery Round by [Andar].

8.2

Indemnify [Brambles] from and against all actions, claims, demands, losses, damages, proceedings, compensation, costs, charges and expenses for which [Brambles] shall or may be or become liable whether during or after the currency of the Agreement and any variation renewal or extension in respect of or arising from –

8.2.1 loss damage or injury from any cause to property or person occasioned or contributed to by the neglect or default of [Andar] to fully, duly, punctually and properly pay, observe and perform the obligations, covenants, terms and conditions contained in the Agreement and on the part of [Andar] to be paid, observed and performed.

8.2.2 loss, damage, injury or accidental death from any cause to property or person caused or contributed to by the conduct of the Delivery Round by [Andar].

8.2.3 loss, damage, injury or accidental death from any cause to property or person occasioned or contributed to by any act, omission, neglect or breach or default of [Andar].

[N]otwithstanding that any of such actions, claims, demands, losses, damages, proceedings, compensation, cost, charges, and expenses shall have resulted from any act or thing which [Andar] may be authorised or obliged to do under the Agreement and notwithstanding that any time waiver or other indulgence has been given to [Andar] in respect of any obligation of [Andar] under the Agreement AND PROVIDED ALWAYS it is agreed and declared that the obligations of [Andar] under this Clause shall continue after variation or termination of the Agreement and any renewal or extension in

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respect of any act, deed, matter or thing happening before such termination.'

At first instance, the jury found in favour of Mr Wail against Brambles. It was held that Brambles negligently caused his injuries. The claim for contractual indemnity by Brambles against Andar was dismissed by Kent J.

Brambles appealed to the Court of Appeal which, while dismissing the appeal against the jury verdict, upheld the contractual indemnity in favour of Brambles. It was held that Brambles was entitled to contribution towards the verdict from Andar, due to the negligence of Andar in respect of Mr Wail's injury. However, the existence of the contractual indemnity made it unnecessary to consider the contribution claim. The effect of the Court of Appeal decision was that Andar was liable for all damages payable to Mr Wail, despite the finding that Brambles was also to blame for the injury.

The Court of Appeal found that there was no justification to read down the indemnity clauses. Andar appealed this decision to the High Court.

In considering the construction of the indemnity clauses, the High Court turned to the principles of construction applicable to contractual guarantees, given that guarantees and indemnities are both designed to satisfy a liability owed by someone (other than the guarantor or the indemnifier) to a third person.

The leading decision on the construction of guarantees is *Ankar Pty Limited v National Westminster Finance (Australia) Ltd*,[2] which held that ambiguous contractual provisions should be construed in favour of the surety (who is in an analogous position to the subcontractor in respect of an indemnity). The High Court found that the law as enunciated in *Ankar* remained the position in Australia.

This is different to the position in the US, which echoed the English Court of King's Bench decision in *Mason v Pritchard*,[3] that the terms of a guarantee 'were to be taken as strongly against the party giving ... as the sense of them would admit it'. The rationale for this approach appeared to lie in circumstances where the instrument was prepared and drafted by the guarantor.

The majority in the High Court in *Andar* (Gleeson CJ, McHugh, Gummow, Hayne and Heydon JJ) turned to the phrasing of the indemnity clauses at 8.2.2 and 8.2.3 of the contract and found that those clauses did not expressly provide that liability arising on the part of Brambles in respect of their negligence fell within the terms of the indemnity.

Rather, the clauses contained two elements:

1. an injury suffered by a 'person'; and
2. the injury be occasioned, or contributed to, by the conduct of Andar.

These elements suggested that the person mentioned in the first element had to be different to the second element; that is, the first person had to be a third party to Andar and Brambles. It was found that, due to Mr Wail's involvement as a director of Andar, he was not such a third party. Therefore, Andar was not liable to indemnify Brambles in respect of Mr Wail's damages awarded against Brambles.

This interpretation was considered to be consistent with clause 4.6 of the agreement, in that the indemnity did not extend to liabilities arising from the operation of the truck, which were attributable to the negligent acts or omissions of Brambles.

Callinan J was of a different view. He did not dispute that indemnity clauses should be strictly interpreted, or that where there is ambiguity, the clause should be construed *contra proferentem*. However, Callinan J thought that there was a very clear indication of the parties' intention that Brambles was to have no liability with respect to claims arising out of the performance of the contract by the Andar, except for a case within the narrow category of instances with which clause 4.6 was concerned.

Andar is authority for the proposition that indemnity clauses must expressly and clearly transfer liability to the extent of liability caused by the head contractor's negligence, to be effective in that regard. In the event that the clause is ambiguous to any extent, it is to be read down to the benefit of the subcontractor.

The NSW Court of Appeal applied the decision in *Andar* in *F & D Normoyle Pty Limited v Transfield Bouygues Joint Venture etc.*[4]

Mr Vranjkovic sustained injury when he tripped on some pipes and fell in the course of his employment with >>

Chadwick Building System on the Transfield construction site of the Sydney Airport domestic terminal railway station. The pipes were left in position by Normoyle for Chadwick to install at some later stage.

Mr Vranjkovic sued Transfield for damages, and Transfield joined both Normoyle and Chadwick, first on the basis that they were joint tortfeasors, and alternatively claiming contractual indemnity under their subcontract agreements.

At first instance, Transfield's claim against the subcontractors was upheld, on the basis of the indemnity clauses in their contract. However, the NSW Court of Appeal overturned this decision, with reference to the principles outlined in *Andar*.

The relevant indemnity clause transferred liability 'arising out of any act, neglect or default' of the subcontractors. As the subcontractors were not part of the cause of the injury by way of breach of duty, breach of contract, or breach of statutory duty, the indemnity did not extend.

To be effective, indemnity clauses must expressly and clearly transfer liability to the extent of liability caused by the head contractor's negligence.

The most recent decision in respect of indemnity clauses has been the case of *Erect Scaffolding (Australia) Pty Limited v Sutton*.[5]

Ian Sutton was injured on a worksite on 21 October 2002, when he struck his head on a crossbar used to support the scaffolding. He commenced proceedings against Australand, the head contractor, and Erect Safe Scaffolding, a subcontractor engaged to provide the scaffolding services. Australand sought indemnity from Erect Safe under the indemnity and insurance clauses in the subcontract.

Clause 11 of the subcontract provided as follows:

'The Subcontractor must indemnify Australand Constructions against all damage, expense (including lawyers' fees and expenses on a solicitor/client basis), loss (including financial loss) or liability of any nature suffered or incurred by Australand Constructions arising out of the performance of the Subcontract Works and its other obligations under the Subcontract.'

Australand was successful at first instance, but the decision was overturned by the NSW Supreme Court of Appeal by a two-thirds majority.

It was held that the word 'arising' confined the scope of Erect Safe's liability to indemnify Australand to damage caused by Erect Safe. It did not extend to indemnify Australand in respect of damage caused by its own negligence.

Basten JA stated that:

'Erect safe's obligation to take out public liability insurance, in so far as that insurance covered Australand, was intended, in the absence of any indication to the contrary, to be co-extensive with its obligations to indemnify Australand. It follows that the clauses should be read together and the construction of one may be influenced by the construction of the other.'

As such, it was also held that there was no obligation for Erect Safe to take out insurance in the name of Australand to cover liability arising from the negligence of Australand.

WHAT WORDING WILL SUCCEED IN TRANSFERRING LIABILITY?

In the South Australian case of *Action Engineering Pty Limited v Press*,[6] Mr Press was awarded damages as a result of the negligence of BHP and Action. BHP successfully enforced the indemnity in its contract with Action, such that Action was ultimately responsible for all of the damages.

The indemnity clauses in the contract were stated in broad terms, inclusive of:

'The Contractor shall be solely liable for and shall indemnify and hold harmless the Company, its officers, employees and agents from and against all liability, damage, loss, expense, costs and proceedings of any nature whatsoever or however arising in or in connection with the Contract, and however or by whosoever caused whether as a result of or arising from negligence, breach of duty or breach of statute by the Company, its officers, employees or agents, or otherwise.'

The relevant indemnity clause was not ambiguous as to whether it extended to create a liability in the subcontractor including to the extent of the head contractor's negligence, and was therefore successful in transferring liability in that regard.

CONCLUSION

The High Court decision in *Andar* provides authority for the proposition that if a contractual indemnity clause does not expressly transfer liability to the extent of the head contractor's negligence, then the indemnity will be read down and the parties will be liable to the extent of their breach of duty of care, statutory duty, or breach of contract.

Andar and the subsequent case law clearly indicate that indemnity clauses need to be carefully drafted to have their desired effect. ■

Notes: **1** [2004] HCA 28. **2** [1987] HCA 15. **3** (1810) 12 East 227. **4** [2005] NSWCA 193. **5** [2008] NSWCA 114. **6** [2006] SASC 207.

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