

NSW: Defending Indemnity Claims



CRISP
LAW

Newsletter

August 2024: Issue 2



In this Newsletter, we discuss the how to defend an indemnity claim brought against a party in a construction contract.

Introduction

An indemnity clause is a provision included in a contract where one party (the indemnifying party) makes a promise or guarantee to the other party (the indemnified party) that they will be free from any liability or loss suffered as a result of an action, inaction or specific circumstance during the performance of a contract.¹

Where a cause of action covered by an indemnity clause arises and imposes an obligation on one party to indemnify the other party, it is important that the indemnifying party knows how to defend themselves against an indemnity claim.

This newsletter will examine how a court will approach an indemnity claim by analysing the way that it is drafted with regards to the contract as a whole and look at how an indemnity claim may be defended where the clause has not been drafted properly and is considered ambiguous.

Importance and relevance of this Newsletter

This newsletter is relevant to key participants in the construction industry who enter into construction contracts as they may be subject to an indemnity claim as some stage and must understand what it is.

The insertion of an indemnity clause allows for the allocation of risk where certain events occur. While it can be advantageous to one party, it will be damaging to the indemnifying party if they become liable to compensate the indemnified party. It may also result in the indemnifying party unknowingly contracting out of defences that they may have had under common law.

As such, this newsletter is important as it will allow key parties such as Contractors and Subcontractors to be aware of how the court will interpret an indemnity clause and give guidance on how this may assist in defending an indemnity claim.

What is an Indemnity clause?

In the High Court case of *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245, an indemnity was described as “a promise by the promisor that he will keep the promisee harmless against loss as a result of entering into a transaction with a third party”.²

¹ Alan Cullen, ‘Building Contracts Australia – Indemnities’ (Lexus Advance, May 2024) <<https://advance.lexis.com/document/?pdmfid=1201008&crd=25d63db2-fd07-4cd9-900e-885ce756cc9d&pddocfullpath=%2Fshared%2Fdocument%2Fanalytical-materials-au%2Furn%3AcontentItem%3A5H4X-F2R1-FG68-G0XG-00000-00&pdcontentcomponentid=267911&pdteaserkey=sr0&pdicsfeatureid=1517127&pditab=allpods&ecom p=hwtpk&earg=sr0&prid=324f6fb9-447b-471f-8ea6-cddc03244eb1>>.

² *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245.

A party that is found to be liable under an indemnity clause will be required to pay the indemnified party for any losses that are covered by the indemnity clause.³

It was outlined in the case of *Andar Transport Pty Ltd v Brambles Ltd* (2014) 217 CLR 424 that an indemnity clause is designed to “satisfy a liability owed by someone other than the guarantor or indemnifier to a third person”.⁴

How to defend an indemnity claim

In order to defend an indemnity claim, it is important that Contractors and Subcontractors understand the terms of the indemnity provision subject to the claim and take appropriate measures where a claim is made against them.

The following are examples of how one party can defend an indemnity claim based on the way a clause was drafted:

Ambiguity

For an indemnity clause to operate effectively, care must be taken in the drafting to ensure that it is unambiguous. Where an indemnity clause is not clear and is open to interpretation, the indemnifying party can defend the indemnity claim on the basis that the clause was ambiguous.

Andar Transport Pty Ltd v Brambles Ltd (Andar Transport)

In the case of *Andar Transport*, the court explained how they will deal with a clause that involves ambiguity. Justice Kirby stated:

- [68] Indemnity clauses are provisions that purport to exempt one party from civil liability which the law would otherwise impose upon it. They are provisions that shift to another party the civil liability otherwise attached by law to the first party. Self-evidently this is a serious thing to do or to attempt to do. Where such indemnities are said to arise out of contracts which are ambiguous or unclear, it is not unreasonable that their provisions should be construed so that any uncertainty is resolved favourably to the party thereby burdened by legal obligations which would otherwise attach to it.⁵

In this case, due to the ambiguity, the court construed the provisions of the clause in favour of *Andar* and as such, *Brambles* was no longer entitled to receive any indemnity from *Andar* pursuant to the indemnity clause.

³ Minter Ellison, ‘Chapter 19 Indemnities’, *Construction Law Made Easy* (webpage, accessed 16 July 2024) < <https://constructionlawmadeeasy.com/construction-law/chapter-19/indemnities/>>.

⁴ *Andar Transport Pty Ltd v Brambles Ltd* (2014) 217 CLR 424.

⁵ *Andar Transport Pty Ltd v Brambles Ltd* (2004) 217 CLR 424 at [68].

Construed Strictly

According to case law, indemnity clauses are also to be 'strictly' construed.⁶

Samways v WorkCover Queensland & Ors [2010] QSC 127 (Samways)

In discussing the construction of the indemnity clause, the court in the case of Samways stated:

- [66] Such an indemnity clause falls to be construed strictly, and any doubt as to the construction should be resolved in favour of the indemnifier. The doubt may arise not only from the uncertain meaning of a particular expression but from its apparent width of possible application.⁷

This is important as it means that an indemnity claim can be defended where the clause has been drafted 'too widely' and leaves doubt as to its meaning and effect. This case is also authority for the fact that indemnity clauses are to be construed according to their 'ordinary meaning'.

Causal Connection ('Causation')

In defending an indemnity claim, it is important that the indemnity clause is interpreted accurately to determine what indemnity is offered and if there is a causal connection between what is covered under the indemnity clause and the loss suffered.

Erect Safe Scaffolding (Aust) Pty Ltd v Sutton (2008) 72 NSWLR 1

This case concerned the faulty erection of scaffolding which resulted in an injury of an employee. Australand Constructions Pty Limited (the Head Contractor) relied on an indemnity clause to seek to recover damages from Erect Safe Scaffolding Pty Limited (the Subcontractor) where the Subcontractor agreed to indemnify the Head Contractor. The indemnity clause relied upon was as follows:

Clause 11 Indemnity

- 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.

⁶ Ibid at [17]-[23].

⁷ *Samways v WorkCover Queensland & Ors [2010] QSC 127* at [66].

The issue to be determined was if Australand's liability was **arising out of** the performance of the Subcontract Works by Erect Safe.

In interpreting the clause, the court said that it was confined by the term “arising out of”. This is important as the court went on to say:

- [157] In the present case the liability of Australand does not “arise” out of the performance by Erect Safe of any of its contractual obligations. Although it is true that the occasion for the liability of Australand was the erection by Erect Safe of the faulty scaffold, the liability of Australand arises from its own independent act of negligence in failing to maintain an appropriate safety regime for the site.⁸

Construed by reference to contract as a whole

Woolworths Group Ltd v Twentieth Super Pace Nominees Pty Ltd atf the Byrns Smith Unit Trust t/as SCT Logistics [2021] NSWSC 344

Additionally, it is important to note that an indemnity clause will be interpreted with reference to the contract as a whole. Where there is any doubt as to its meaning, the court will construe the clause in favour of the indemnifying party. This is discussed in the following paragraph:

- [26] An indemnity clause... is to be construed by reference to the contract as a whole. Where there is ambiguity and doubt as to the proper construction either from the uncertain meaning of a particular expression or the apparent width of possible application, it might be appropriate to construe an indemnity provision contra proferentem in favour of the indemnifier, although that is a principle of last resort.⁹

Explicit reference to survival

Where a contract has been terminated or completed, an indemnity clause will no longer apply unless there is an explicit reference stating that it will survive termination and completion.

Honeywell Ltd v Acciona Infrastructure Projects Australia Pty Ltd [2023] NSWSC 663

In this case, Lendlease gave an indemnity to Honeywell under an Interface Deed. Clause 5.3 (the indemnity clause) obliged the Contractor to indemnify Honeywell in certain circumstances including where Honeywell “incurs losses, costs, expenses or damages by virtue of ... an act ... of [Novacare] ... to the extent such losses, costs, expenses or damages were caused or

⁸ Erect Safe Scaffolding (Aust) Pty Ltd v Sutton (2008) 72 NSWLR 1.

⁹ Woolworths Group Ltd v Twentieth Super Pace Nominees Pty Ltd atf the Byrns Smith Unit Trust t/as SCT Logistics [2021] NSWSC 344.

contributed to by the Construction Contractor’s act, omission or failure to comply with its obligations arising out of the Construction Contract or this deed.”

The court went on to say at paragraph [8] that:

- [8] the **indemnity is a continuing obligation and survives the expiry or termination of the deed**: clause 24.9(a). That is, the indemnity is not necessarily limited to 12 years after Completion.¹⁰

This is important to be aware of when defending an indemnity claim as the clause may no longer apply.

CONCLUSION AND IMPLICATIONS

Overall, as explained above, a party entering into a construction contract must be cautious when dealing with an indemnity clause and agreeing to indemnify another party.

This newsletter will thus be useful to both parties as it shows the level of detail that must be placed into drafting indemnity clauses where one party seeks to rely on it. This is because the court can decide against the party that was to be indemnified where the clause is inconsistent with the contract, ambiguous and leaves room for doubt.

Where an indemnity claim is made, this can result in negative consequences for the indemnifying party and as such, this newsletter will be helpful in defending an indemnity claim where the indemnified party is relying on a clause that has not been properly drafted.

¹⁰ Honeywell Ltd v Acciona Infrastructure Projects Australia Pty Ltd [2023] NSWSC 663.