

Indemnity: Getting the Money Back

— by Brian S. Ruff

Professor William Prosser in his treatise on torts explained that “Indemnity is a shifting of responsibility from the shoulders of one person to another; and the duty to indemnify will be recognized in cases where community opinion would consider that, in justice, the responsibility should rest upon one rather than the other.” In other words, the professor was saying that the person responsible for making the mess should clean it up.

Under Oregon law, there are various types of indemnity, including contractual and statutory. This article will focus, however, on common law indemnity in situations where there is no formal right to recover spelled out between the parties.

Much has been written about indemnity in the field of construction litigation. However, it is important to realize that indemnity, and in particular common law indemnity, is available in many different circumstances, including cases involving products liability, premises liability and employer liability.

In Oregon, the basic elements of a claim for indemnity are: 1) the indemnity plaintiff has discharged a legal obligation that it owed to a third party, 2) the indemnity defendant is also liable to the third party, and 3) as between the indemnity plaintiff and the indemnity defendant, the obligation ought to have been discharged by the latter. See Fulton Insurance Company v. White Motor Corporation (1972); Genesis Indemnity Insurance Company v. Deschutes County (2004). In the years since Fulton, the Oregon courts have had the opportunity to further clarify those elements, and a substantial body of law concerning indemnity has developed.

The requirement that the indemnity plaintiff must discharge a legal obligation owed to

the third party has been paid particular attention to by the courts. In 2003, the Oregon Court of Appeals explained, in Moore Excavating Inc. v. Consolidated Supply Co., that an indemnity plaintiff must show it discharged both its own and the indemnity defendant’s liability. In other words, before an indemnity defendant will be on the hook for indemnity to an indemnity plaintiff, the indemnity plaintiff must show that it has “bought peace” for the indemnity defendant in a way that is legally binding on the third party.

The biggest hurdle in an indemnity claim, however, is the third element, under which the indemnity plaintiff must prove, as between it and the indemnity defendant, that the indemnity defendant should bear the obligation to the third party. The Oregon Supreme Court stated, in Piehl v. The Dalles General Hospital, that the essential principal of common law indemnity is “the equitable distribution of responsibility,” but also recognized that there was “no all-encompassing rule” to determine which of the parties would be more responsible than the other.

Generally, in analyzing the comparative responsibilities, the discussion has relied upon use of the terms “primary” or “active” liability versus “secondary” or “passive” liability. For instance, in Smith Radio Communications Inc. v. Challenger Equipment Ltd. (1974), a third party was injured as a result of faulty radio equipment. The third party received a judgment against the retailer of the equipment, even though established facts demonstrated that the equipment had been sold by the retailer without modification and in the same condition that it had been received from the manufacturer. The

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retailer then filed suit against the manufacturer for common law indemnity of defense costs and the amount of the judgment. The court found that since the equipment had been delivered by the retailer to its customer without modification, its liability was passive and secondary to that of the manufacturer, whose liability was active and primary. Therefore, the retailer was entitled to indemnity from the manufacturer.

The second element of the analysis, that the indemnity defendant be liable to the third party, has raised problems when the indemnity defendant's liability was not established in the underlying case, particularly in situations where the indemnity plaintiff settles with the third party prior to trial. When the indemnity defendant's liability is established in the underlying case, either by judgment or admission, then it is established for the purpose of the indemnity claim. However, in circumstances where the indemnity defendant's liability is not established in the underlying case, the courts have held that the indemnity plaintiff must establish liability in the indemnity case itself.

The old rule with respect to liability, as stated in Fulton and United State Fire Insurance Company v. Chrysler Motors Corporation (1973), was that the indemnity plaintiff and the indemnity defendant both had to be liable to the third party. However, that rule was changed in Kamyr Inc. v. Boise Cascade Corporation (1974). After Kamyr, an indemnity plaintiff seeking only defense costs was no longer required to prove its own liability, only that of the indemnity defendant.

The new rule eventually led to new line of cases, establishing a common law cause of action for indemnity of costs following a successful defense. Beginning with PGE v. Construction Consulting Associates (1982) and Department of Transportation v. Scott (1982), the Court of Appeals has followed

the Kamyr rule, and has stated that if an indemnity plaintiff had been successful in defending the underlying case and was seeking defense costs only, it need only plead: 1) that it was sued, 2) that it reasonably incurred costs in defending that suit, and 3) that as between it and the indemnity defendant, the indemnity defendant should bear the burden of the defense. Those decisions were reinforced later by Martin v. Cahill (1988).

It is important to note, however, that the new set of elements does not supplant the traditional elements established in Fulton. In Moore Excavating v. Consolidated Supply Co. (2003), the court explained that the indemnity plaintiff seeking defense costs must still show that it has discharged the indemnity defendant's liability to the third party. Therefore, it must be established that the indemnity defendant had some liability to the third party to start with.

This leads to the question, "What about situations where there is no liability at all?" For instance, what about a products liability claim in which a product was found to be not faulty, and a retailer seeks defense costs from the manufacturer anyway? In Valley Industries v. Scott Fetser Co. (1992), the court found that neither the indemnity plaintiff, the indemnity defendant, nor the product was involved in the injury to the third party. Therefore, there was no basis for indemnity, even under the elements established in PGE. The reason for that was the indemnity plaintiff could not prove, as between it and the indemnity defendant, which was more liable than the other.

The no-liability situation is similar to one in which both indemnity parties are equally liable. To borrow one of those Latin phrases that lawyers like so well, the parties would be *in pari delicto*, or equally at fault. As the Court of Appeals stated in Star Mountain Ranch v. Parimoore (1989), "if the parties are *in pari delicto*, indemnity will not lie." It

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stands to reason, that if both parties are equally liable, then the third element cannot be met.

The possibility of indemnity should be kept in mind whenever your insured's actions are passive or secondary as compared to those of another party, and it is always a good idea to tender the defense to the indemnity defendant early in the dispute. You may still be able recover your losses even in the absence of an indemnity contract or applicable statute. If you have satisfied a judgment or paid the costs to successfully defend a claim due to another party's primary actions, you may be able to get the money back. ❖

— *If you have any questions about this subject, please feel free to contact the author at brian@lerlaw.com or 503-768-9600.*