

Implied Indemnity in Virginia and Its Application to Claims for Economic Damages

by Jack Rephan



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The business of construction, of necessity, involves a multitude of parties. These include contractors, subcontractors, material suppliers, owners, architects and others. Risk shifting and risk sharing are the natural products of the construction process. Disputes on a construction project will often involve several parties. Two or more parties may share the responsibility for the problem that caused the damages or added expenses to a party. When the parties involved are unable to resolve their differences, and litigation results, the defending party will often shift to one or more other parties, all or part of any liability the defending party may have to the original plaintiff or claimant.

Most well-drafted contracts for construction should contain indemnity provisions under which one party agrees to indemnify and hold the other party harmless from liability, loss or damages resulting, wholly or partially, from the fault of the indemnitor. The indemnity provision of the contract governs the rights of the party seeking indemnification from the other party if the contract between the parties contains an indemnity provision covering

the type of liability, loss or damage for which indemnity is sought. Otherwise, the party seeking to shift his responsibility or liability to another must rely upon another legal theory to do so.

Contribution and indemnity are legal theories often relied upon to shift all or part of one party's liability to a third party to another party. In Virginia, there is a right of contribution between joint tortfeasors for liability for personal injury caused to a third party or for damage done to the property of a third party. At common law, there was no right of contribution between joint tortfeasors. Statute created this right and it applies only to injury to person or property resulting from negligence.¹ To establish a right of contribution, it must be alleged and shown that the party claiming contribution is secondarily or vicariously liable to the injured party and the party, from whom contribution is claimed, is primarily liable to the injured party. Contribution deals only with tort liability.² Consequently, where the damages complained of consist only of economic damages, rather than damages for injury to person or property, no right of contribution exists.

Unlike contribution, indemnity can be for either tort liability or contractual liability. A right of indemnity can be express, contractual or implied. A claim for express indemnity must be based upon a written agreement between the parties under which one party agrees to indemnify and hold the other party harmless for a loss, claim, expense or liability, which the indemnitee may incur or be liable for to a third party. If an express agreement for indemnity exists between the parties covering the liability, loss or damage in question, any right of implied indemnity will be precluded.³ Where there is no expressed agreement of indemnity between the parties, or where the liability, loss or damage against which indemnity is sought is beyond the scope of the written indemnity agreement—if any right of indemnity exists—it must be implied. This brief article will examine the question of whether a substantive right to relief under the theory of implied indemnity exists in Virginia and,

if so, whether implied indemnity will support a right to relief where only economic damages or losses are involved in the claim against which indemnity is sought from another party.

Implied Indemnity Is Recognized in Virginia.

As a general proposition, implied indemnity is recognized in Virginia.⁴ Implied indemnity in Virginia has been compared to the right of contribution among joint tortfeasors where, as stated above, a secondarily or vicariously liable party may seek contribution from the party who is primarily liable for the injury or damage.⁵ However, unlike contribution, indemnity “must necessarily grow out of a contractual relationship.”⁶ Thus, absent contractual relationship between the indemnitor and the indemnitee, implied indemnity will not lie. Moreover, a contractual relationship between the parties will not alone support a claim of implied indemnity. An implied right to indemnification can be found only in two sets of circumstances. First, an implied right to indemnification may arise because of the special nature of the contractual relationship between parties. Second, a right to indemnity may be found in what has been called “implied in law” indemnity. This is a tort-based right to indemnification where there is a great disparity in the fault of two tortfeasors, and a tortfeasor has paid for, or is liable for, a loss that was primarily the responsibility of the other.⁷

Most all of the Virginia cases allowing claims of implied indemnity have involved personal injuries or damages to property and, therefore, fall within the “implied in law” category. Since liability for injury to persons or property can arise absent any privity of contract with the injured party, these cases do not offer much support for a claim of implied indemnity against liability for purely economic damages.

Most construction litigation involves only claims for economic damages and only contract law. Because the legal principles applicable to claims for economic damages differ greatly from those applicable to

claims for personal injury or property damage, it is important to make a distinction between those cases in which indemnity was sought against liability for injury to person or property and those cases in which indemnity was sought against liability for economic damages. In the normal construction setting, the relationships between various parties arise only by virtue of the contractual arrangements between them. There are no special relationships among the various parties that arise as a matter of law, such as those that may cause tort liability for injury to person or property, or obligations imposed by statute and for which privity of contract is not required. Whatever duties the parties have to each other exist only by virtue of the terms of the contract between them.

Unlike the situation where indemnity is sought against liability for personal injury or damage to property, where implied indemnity is sought against liability for purely economic damages, the economic loss doctrine can create an insurmountable obstacle to establishing a right of recovery under an implied indemnity theory. An application of the economic loss doctrine may insulate a prospective third party indemnitor from liability to the party suffering the economic loss due to an absence of privity of contract between such parties, thus making it impossible to satisfy what is an essential element of implied indemnity.

Virginia Law Requires that the Party from whom Indemnity is Sought be the Party Primarily Liable to the Injured Party.

As with the right of contribution among joint tortfeasors, the principle that no right of contribution exists unless the party from whom contribution is sought is liable to the original plaintiff, has been held to be equally applicable to implied indemnity.⁸ “The right to indemnity or exoneration for a base must rest upon the fact that the party seeking indemnity has discharged, under contractual obligation, expressed or implied, the obligation of the one primarily liable.”⁹ One court has stated: “Without exception, the courts have held that,

under Virginia law, the right to non-contractual indemnity arises only when the party from whom liability is sought may be liable in tort to the original plaintiff.¹⁰ It

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follows, therefore, that it is not sufficient to show that a party has breached some duty owed only to the party claiming indemnity, but it must be shown that the damages were caused by a breach of some obligation owed to the original plaintiff as well.¹¹ This important element for alleging and proving a claim based on implied indemnity is often misinterpreted to mean that it is only necessary to allege and prove that the party from whom indemnity is sought primarily caused the damages against which indemnity is claimed.

The fact that the prospective indemnitee primarily caused the damages claimed by the original plaintiff is not enough; the prospective indemnitee must be at least potentially liable to or has breached some duty owed to the original plaintiff as well, and, if such liability is precluded, either as a matter of law, or for any reason, implied indemnity cannot be claimed. Although claims of implied indemnity have been allowed in cases involving injuries to persons or property, in these cases, the putative indemnitor was potentially liable to the original plaintiff, either for negligence or for breach of warranty. However, indemnity has been denied, for example, where the putative indemnitor was insulated from liability to the original plaintiff due to the exclusivity of the Workers' Compensation Act of Virginia,¹² or the Longshoremen's and Harbor Workers' Compensation Act.¹³ Similarly, neither contribution nor indemnity could be

claimed from the United States Government for liability for injuries to members of the Army Reserve sustained while on training because the government

could have no liability to the plaintiffs under the Federal Torts Claim Act.¹⁴

The writer in his research has been unable to find any reported decision in Virginia allowing a claim of implied indemnity against liability for purely economic loss or damage based upon a finding that an implied agreement of indemnity existed between the parties simply by virtue of their contractual relationship.¹⁵ The cases that allowed a claim of implied indemnity based on the special nature of a contractual relationship between the parties, or the so called “implied contract theory,” all involved claims for personal injury or property damage based upon negligence, breach of warranty or the assumption, by operation of law or by contract, of some duty owed by the indemnitee to the injured party.

Current Virginia Law Indicates that There is No Implied Indemnity Against Liability for Economic Damages Absent Liability of the Indemnitor or a Breach of Some Duty Owed to the Injured Party.

Because a claim of implied indemnity must rest upon a breach of some duty owed by an indemnitor to the original claimant for which the party claiming a right of indemnity may be liable, it logically follows that there can be no right of implied indemnity in Virginia for purely

economic damages unless the indemnitor has, by contract or otherwise, assumed a duty owed to the injured party, a breach of which caused the injured party's damages.¹⁶ Based upon existing Virginia case law, it does not appear that a right of indemnity against economic losses or damages can be implied solely from the contractual undertakings in a normal contract for construction that does not contain some language manifesting an agreement to hold another party harmless against liability to a third party for economic damages or loss. Another obstacle to seeking implied indemnity against a claim for purely economic damages is that the typical express indemnity clause found in many of the more widely used prime and subcontract agreements provides for indemnity only against claims for bodily injuries or damage to property. A court may very likely hold that any claim of implied indemnity against economic damages is excluded by such provision under the doctrine of *expressio unius est exclusio alterius*.

The parties involved in a construction project resort to contract and contract law to protect their economic expectations. Their special rights and duties are defined by the contracts they reach. Protection against economic losses caused by another's failure to perform properly is but one provision a contractor may require in striking his bargain. Any duties in this regard arise purely by reason of the contractual relationship between the parties.¹⁷ Even a breach by one party of its contractual obligation will not, by itself, give rise to a claim for implied indemnity against a claim by a third party for economic damages. The well established common law rule in Virginia is that a party not in privity with another may not recover damages for “purely economic loss,” but only for physical injury to personal property.¹⁸ Virginia law shows that an essential element of a claim of implied indemnity is that the prospective indemnitor is liable to, or has breached a duty owed to, the original plaintiff for all or a portion of the damages claimed against the prospective indemnitee, where the damages being claimed by the original plaintiff consist of

“purely economic loss.” Therefore, any claim of implied indemnity will, in all probability, be precluded by the economic damage rule.

Procedural Rules Allowing Third Party Actions do not Create a Right of Action for Implied Indemnity.

Procedurally, in a state court action in Virginia, a party desiring to bring in another party as a third party defendant is allowed to do so under Virginia Code §8.01-281 and Rule 3:10 of the Rules of the Supreme Court of Virginia. Third party practice in a federal court is also permissible under Rule 14(a) of the Federal Rules of Civil Procedure, which is virtually identical to Rule 3:10. However, these rules are only procedural and do not create any right to relief. There must exist a right to relief under applicable substantive law¹⁹—“an action does not become an action for indemnity merely because the pleader has so denominated it.”²⁰

Because a substantive cause of action must exist independently of the procedural rules allowing a claim for indemnity to be asserted against a third party, careful consideration should be given to whether any right of implied indemnity exists against a third party before attempting to assert a third party claim for indemnity against that party. A third party motion for judgment or complaint merely alleging that the third party was the party causing the injury or damage, in whole or in part, may not survive a demurrer or a motion to dismiss failure to state a cause of action. This better practice would be to allege facts sufficient to show that a right of action for indemnity does exist. If the subject matter of the claim for indemnity consists of a claim solely for economic

damages or loss, then it is essential to allege and prove, if possible, that the third party defendant owes some duty, contractual or otherwise, to the original plaintiff a breach of which caused, in whole or in part, the plaintiff’s injury or damage.

Conclusion

To succeed on a claim of implied indemnity, existing authorities in Virginia strongly suggest that it must be alleged and proved that the party from whom indemnity is sought is the one primarily liable for the damages caused to the original plaintiff and the party claiming indemnity must only be secondarily liable. Absent a breach of some duty owed to the original plaintiff, or where any liability to the original plaintiff is precluded by some rule of law, the current state of Virginia law suggests that no right of implied indemnity exists. This critical element is often overlooked in the construction setting where there is no express agreement of indemnity between the parties involved covering not only indemnity against liability for personal injuries and property damage, but also liability to third parties for economic damages. Damages being claimed that consist of “purely economic loss,” in any right of implied indemnity may be precluded under Virginia law. The importance of a well-drafted express agreement of indemnity should, therefore, never be overlooked. ☞

Endnotes

- 1 Virginia Code § 8.01-34.
- 2 Virginia Code § 8.01-34. See also *Hartford Accident & Indemnity Co. v. Williams*, 291 F. Supp. 103 (W.D. Va. 1968).
- 3 *Fidelity & Deposit Co. of Md. v. Bristol Steel Iron Works, Inc.*, 722 F.2d 1160, 1163 (4th Cir. 1983).
- 4 *Sykes v. Stone & Webster Eng. Corp.*, 186 Va. 116, 41 S.E.2d 469 (1947); *Sanderling v. Donohoe Co.*, 42 Va. Cir. 345 (Fairfax County 1998); *VEPCO v. Wilson*, 221 Va. 979, 277 S.E. 2d 149 (1981).

- 5 *Jennings v. Franz Torwegge Machine Works*, 347 F. Supp. 1288 (W.D. Va. 1972); *Oman v. Johns-Mansville Corp.*, 482 F. Supp. 1060 (E.D. Va. 1980), aff’d, *White v. Johns-Mansville Corp.*, 662 F.2d 243 (4th Cir. 1981).
- 6 *VEPCO v. Wilson*, 221 Va. at 981-82; *Jennings v. Franz Torwegge Machine Works*, 347 F. Supp. at 1288.
- 7 *International Surplus v. Marsb & McLennan, Inc. v. City of Richmond*, 838 F.2d 124,126 (4th Cir. 1988). See *Ryan Stevedoring Co. v. Pan-Atlantic S.S. Corp.*, 350 U.S. 124, 76 S. Ct. 232, 100 L. Ed. 133 (1956) and *General Electric Co. v. Moretz*, 270 F. 2d 780 (4th Cir. 1959) cert. denied, 361 U.S. 964 (1960). In *Ryan*, the Supreme Court held that a shipowner has an implied contractual right to indemnity for damages paid to an injured longshoreman where a stevedoring company had agreed to perform all the shipowner’s stevedoring operations and, because of non-delegable duties imposed in maritime law by the seaworthiness doctrine, the stevedoring company’s negligent injury of the longshoreman was also a breach of its contractual duties to the shipowner. In *Moretz*, the 4th Circuit found that under Virginia law, certain relevant federal statutes and regulations should be read into a contract between a shipper and a carrier and these provisions established a special contractual relationship that supported the shipper’s claim for implied indemnity for injuries caused to a truck driver due to the negligence of the shipper in loading the truck.
- 8 *VEPCO v. Wilson*, 221 Va. at 981; *Jennings v. Franz Torwegge Machine Works*, 247 F.Supp. at 1288; *Oman v. Johns-Mansville Corp.*, 482 F. Supp. at 1060.
- 9 *Sykes v. Stone & Webster Eng. Corp.*, 186 Va. at 129, quoting 42 Corpus Juris Secundum 564; 27 Am. Jur., 456-457(465-6); *Mabone v. McGraw-Edison Co.*, 281 F. Supp. 582 (E.D. Va. 1968) and *Drumgoole v. VEPCO*, 170 F. Supp. 824 (E.D. Va. 1959).
- 10 *Glover v. Johns-Mansville Corp. v. United States*, 525 F. Supp 894 (E.D. Va 1979), citing *Jennings v. Franz Torwegge Machine Works*, *supra* and *Drumgoole v. VEPCO*, *supra*.
- 11 *International Surplus Lines Insurance Co.*, 838 F.2d at 124. See also *Moretz v. General Electric Company*, 170 F. Supp. 698 (W.D. Va. 1959); *Oman v. Johns-Mansville Corp.*, 482 F. Supp. at 1060; *Pierce v. Martin ex rel. Commercial Union Insurance Co.*, 230 Va. 94, 96-97, 334 S.E.2d 576 (1985); *VEPCO v. Wilson*, 221 Va. at 981.
- 12 *McGraw-Edison Co. v. W.L. Wachter Electrical Contractor, Inc.*, 281 F. Supp. 582 (E.D. Va 1968).
- 13 *Oman v. Johns-Manville Corp.*, *supra*.
- 14 *Drumgoole v. VEPCO*, *supra*.
- 15 Corbin on Contracts, Vol. 5, § 1037, pp. 190, 191, quoted by the Virginia Supreme Court in *Hiss v. Friedberg*, 201 Va. 572, 112 S.E. 2d 891 (1960), suggests that, where it can be shown that the defendant’s breach of contract caused litigation involving the plaintiff that resulted in the payment of counsel fees, court costs, and the amount of a judgment, and such expenditures are reasonable, plaintiff can recover damages measured by these expenditures. However, *Hiss* dealt only with the question of whether plaintiffs could recover their counsel fees in a prior action made necessary or caused by defendants’ breach of contract. Whether *Hiss* would support a claim, couched in terms of consequential damages for breach of contract, where the damages consist of, in reality, a claim for indemnity against actual or



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- these authors discussing this topic appears in the winter edition of the Construction Lawyer, of the ABA Forum on Construction.
- 2 *The New York Times* noted in its October 1, 2002, business section at p. C1 that, "The sinking feeling that gripped the American stock market caused the Standard and Poor's index of 500 stocks to plunge 17.6 percent, its worst quarterly showing since the market crashed in late 1987." *The Wall Street Journal* noted on September 30, 2002, that industrial stocks were at their lowest point in four years, hammered by persistent worries about an unsteady economic recovery.
 - 3 *Los Angeles Business Journal*, August 26, 2002, p.24
 - 4 Hamilton & Trautmann, SARBANES-OXLEY ACT OF 2002 LAW AND EXPLANATION (CCH, Inc. 2002) (hereinafter "Hamilton").
 - 5 *Financial Times*, August 22, 2002, p. 27.
 - 6 148 *Cong. Rec.* S7350-04.
 - 7 *The New York Times* predicted [correctly] the likely indictment of former CFO of Enron, Andrew S. Fastow, in connection with criminal fraud in connection with his role in such off-balance-sheet transactions, noting that these activities "might prove to be the most explosive element of a raft of allegations that the government is expected to bring against Mr. Fastow." p. C1 (October 1, 2002).
 - 8 Kaplan & Hannapel, "Life After Sarbanes-Oxley—Hear the Whistle Blow," *Legal Times*, P.32 (October 7, 2002).
 - 9 For an excellent and concise summary of the new criminal penalties, See, W. Warren Hamel, Thomas J. Kelly, Jr., Kathleen S. Dolan, "Life After Sarbanes—They Got Tougher," *Legal Times*, p. 34 (October 7, 2002).
 - 10 *Engineering News Record* (ENR), "News Site: Management: Governance Rules Touch Industry," August 12, 2002, pp. 10-11.
 - 11 *Ibid.*
 - 12 *Id.* at 11.
 - 13 Andrew J. Sherman, "Corporate Governance and Reporting in the new age of Scrutiny: Implications for Both Public and Privately-Held Companies," Wingman Center for Entrepreneurship, University of Maryland, (October 31, 2002) (unpublished).
 - 14 *Id.*, at 7.
 - 15 *Ibid.*
 - 16 *Supra*, n. 10, at 11.
 - 17 24 *New York Law Journal*, p. 9 (August 22, 2002).
 - 18 *Supra*, n. 10, at 11.
 - 19 Kaplan & Hannapel, "Life After Sarbanes-Oxley—Hear the Whistle Blow," *Legal Times*, P.32 (October 7, 2002)
 - 20 *Ibid.*
 - 21 *Ibid.*
 - 22 *Ibid.*
 - 23 For an interesting article discussing this dilemma, see Tambe, Redgrave 17 *Washington Legal Foundation Legal Backgrounder* (August 9, 2002) No. 31. Interestingly, on December 4, 2002, *The Washington Post* reported that five Wall Street companies had agreed to pay \$1.65 million each to the SEC for failing to properly save e-mail. *Wash. Post*, December 4, 2002, p. B-1.
 - 24 204 F.R.D. 277, 201 U.S. Dist. LEXIS 18824 (E.D. Va. 2001).
 - 25 *Supra*, n. 24.

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- potential liability for purely economic damages, is unclear.
- 16 One or two cases have arisen in claims for breach of express or implied warranties under the Uniform Commercial Code. See *Whittle v. Timesavers, Inc.* 572 F. Supp. 584 (W.D. Va. 1983); and *Wingo v. Celotex Corp.*, 834 F.2d 375 (4th Cir. 1987). Both of these cases involved claims for personal injuries based upon the theories of negligence and breach of warranty. Unlike cases involving claims for purely economic damages, a lack of privity does not insulate the proposed indemnitor from liability to the original plaintiff for injury to person or property, either under a negligence or a breach of warranty theory. Also, the lack of privity is no defense under Virginia Code § 8.2-318 to an action against a manufacture or seller of the goods for breach of warranty or for negligence resulting in an injury to person or to property. Therefore, the requirement that the proposed indemnitor be liable to or owed a duty to the original plaintiff was met in these cases. They offer questionable support for a claim of implied indemnity against liability for purely economic damages. Although a lack of privity does not bar of claim for direct damages for breach of warranty under the UCC, under *Beard Plumbing & Heating v. Thompson Plastics*, 254 Va. 240, 491 S.E. 2d 731 (1997), "economic consequential damages" are precluded where no privity exists so it must be presumed that implied indemnity will not lie against liability to a third party for this type of damages.
 - 17 See *Richmond Metro Authority v. McDevitt St. Bovis, Inc.*, 256 Va. 553,507 S.E. 2d 344 (1998), to the effect that the negligent performance of a duty imposed upon a party by contract is not actionable in tort absent a corresponding common law duty. *cf. Accordia of Virginia Ins. Agency, Inc. v. Genito Glenn, L.P.*, 263 Va. 377, 560 S.E. 2d 246 (2002), upholding the trial court's submission of a negligent performance of a contract claim for economic loss damages to the jury where privity existed between the parties.
 - 18 *Sesenbrenner v. Rust, Orling & Neale, Architects, Inc.* 236 Va. 419, 374 S.E. 2d 55 (1988); *Blake Const. Co. v. Alley*, 233 Va. 31, 353 S.E.2d 724 (1987).
 - 19 *Valley Landscape Co. v. Rolland*, 218 Va. 257, 237 S.E.2d 120 (1977); *Virginia Int'l Terms., Inc. v. Chesapeake Marine Terms., Inc.*, 879 F. Supp. 31 (E.D.Va 1995).
 - 20 *International Surplus Lines Ins. Co. v. Marsb & McLennan, Inc.*, 838 F.2d 124, 126 (4th Cir. 1988), quoting *Peoples' Democratic Republic of Yemen v. Goodpasture, Inc.*, 782 F.2d. 346 (2nd Cir. 1986).