22 CONSTRUCTION CONTRACT LITIGATION

Much of the litigation involving construction contracts pertains to the interpretation and effect of contract provisions. In Alaska, the court will apply the reasonable expectations of the parties standard (i.e., the sense in which the party using the words should reasonably have apprehended that they would be understood by the other party).[1]

Indemnification clauses (discussed at Tab 10 -- Indemnity) provide a method of shifting project risks from one party to another. These clauses are valid in Alaska except where indemnification would tend to promote a breach of public policy.[2] The public policy exception is applicable where the duty to perform is one owed to the public at large.[3] This typically occurs where one of the parties is a public utility or a common carrier.[4]

In addition to shifting responsibility for the payment of any damages that may be awarded to the claimant, an express indemnity provision will allow the promisee to recover its full attorney's fees and costs.[5]

AS 45.45.900 declares that any construction contract provision purporting to exculpate the promisee from its own liability for damages arising from the sole negligence or willful misconduct of the promisee (including the promisee's agents or independent contractors) is against public policy and is therefore void and unenforceable. However, this **statute only applies when the indemnitee is solely negligent**.[6] These clauses are not *per se* unenforceable, but instead have been interpreted to bar indemnity based on the indemnitee's sole negligence. This is a determination of fact for the trier of fact, and until such determination has been made, the indemnitor may have a duty to defend. This duty is separate from the duty to indemnify and arises when a claim within the scope of the indemnity clause is made

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[1] *Day v. A & G Constr.*, 528 P.2d 440, 445 (Alaska 1974).

[2] *Burgess Constr. Co. v. State*, 614 P.2d 1380 (Alaska 1980).

[3] *Manson-Osberg Co. v. State*, 552 P.2d 654 (Alaska 1976).

[4] *Northwest Airline v. Alaska Airlines*, 351 F.2d 253 (9th Cir. 1965).

[5] *Heritage v. Pioneer Brokerage & Sales*, 604 P.2d 1059 (Alaska 1979).

[6] *Rogers & Babler v. State*, 713 P.2d 795 (Alaska 1986); *see also* 1986 Informal Op. Att'y Gen. 165; *see also City of Dillingham v. CH2M Hill Northwest, Inc.*, 873 P.2d 1271 (Alaska 1994) (limitation of liability clause prohibited under AS 45.45.900).

requiring a defense. The duty to indemnify does not arise until the indemnitee is liable for damages.[7]

Arbitration clauses are favored in Alaska as a means of resolving disputes without court interference but the parties will likely have no right to appeal the arbitrator's decision in the absence of fraud, corruption, or gross negligence during the arbitration.[8] Liquidated damages clauses have also been upheld as valid in Alaska.[9]

As in other types of contract disputes, only those damages which are reasonably and foreseeably caused by the breach, and that can be proven with reasonable certainty, are recoverable. Accordingly, damages in construction contract litigation should be proven using some form of the "actual cost" method, in which each element of extra expense incurred because of the breach is added together for a total claim.[10] A "total cost" approach to proving damages, in which the contractor attempts to prove its damages by the difference between its expected costs and its actual costs, is strongly disfavored.[11] The reason for disfavoring a total cost method is its assumption that all of the additional cost is caused by the defendant's breach of contract. Other methods of estimating damages that use these same types of assumptions are also disfavored, even though they may not be denominated "total cost" methods.[12] A "total cost" method, however, may be used to prove damages under limited circumstances. The contractor must affirmatively show four elements before being permitted to use a total cost approach: 1) that these particular types of losses are impossible or highly impracticable to determine with a reasonable degree of accuracy, 2) that its bid was reasonable, 3) that its actual costs were reasonable, and 4) that it was not responsible

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[7] *Hoffman Constr. Co. of Alaska v. U.S. Fabrication & Erection, Inc.*, 32 P.3d 346 (Alaska 2001).

[8] *Alaska State Hous. Auth. v. Riley Pleas,* 586 P.2d 1244 (Alaska 1978).

[9] *Industrial Indem. Co. v. Wick Constr. Co.*, 680 P.2d 1100 (Alaska 1984).

[10] *Anchorage v. Frank Coluccio Constr. Co.*, 842 P.2d 316, 325 (Alaska 1992).

[11] *Fairbanks North Star Borough v. Kandik Constr.*, 795 P.2d 793, 798-99 (Alaska 1990); *see also Frank Collucio Constr.*, 842 P.2d at 325.

[12] *Geolar v. Gilbert/Commonwealth*, 874 P.2d 937 (Alaska 1994).

for the added expenses.[13] Total cost estimation of damages is available only as a "last resort."

Appendices:

AS 45.45.900

[13] *Collucio*, 842 P.2d at 325.

Article 10. Miscellaneous Provisions.

Sec. 45.45.900. Indemnification agreements against public policy. A provision, clause, covenant, or agreement contained in, collateral to, or affecting a construction contract that purports to indemnify the promisee against liability for damages for (1) death or bodily injury to persons, (2) injury to property, (3) design defects or (4) other loss, damage or expense arising under (1), (2), or (3) of this section from the sole negligence or wilful misconduct of the promisee or the promisee's agents, servants or independent contractors who are directly responsible to the promisee, is against public policy and is void and unenforceable; however, this provision does not affect the validity of an insurance contract workers' compensation, or agreement issued by an insurer subject to the provisions of AS 21, or a provision, clause, covenant, or agreement of indemnification respecting the handling, containment or cleanup of oil or hazardous substances ad defined in AS 46. (§ 1 ch 155 SLA 1975; am § 6 ch 59 SLA 1986)

Revisor's notes. — Formerly AS 45.47.010. Renumbered in 1980.

Opinions of attorney general. — The apparent prohibition on indemnification agreements in construction contracts found in this section will only apply when the promissee is completely negligent and seeks to hold an innocent promisor accountable. February 27, 1986 Op. Att'y Gen.

Legislative intent. — The absence in this section of an exemption for limitation of liability clauses indicates that the legislature did not intend to allow an exemption. City of Dillingham v. CH2M Hill N.W., Inc., 873 P.2d 1271 (Alaska 1994).

The word "indemnify" as used in this section means "exempt," and thus this section prohibits limitation of liability clauses; absent legislative action to the contrary, such an interpretation best fulfills the legislature's express intent to prevent a party to a construction contract from bargaining away liability for the party's negligent acts. City of Dillingham v. CH2M Hill N.W., Inc., 873 P.2d 1271 (Alaska 1994).

Applicability of section. — This section became effective on September 23, 1975, and governs contracts executed on or after that date. Contracts executed before that date are governed by the rule announced in Burgess Constr. Co. v. State, 614 P.2d 1380 (Alaska 1980), that an indemnity clause is effective to shift responsibility for an accident where the indemnitee is negligent and the indemnitor is not. Stephan & Sons v. Municipality of Anchorage, 629 P.2d 71 (Alaska 1981).

There is no indication in the text of this section itself that would indicate that the statute is intended to ban only indemnification clauses that would benefit a public promisee at the expense of a private promisor. City of Dillingham v. CH2M Hill N.W., Inc., 873 P.2d 1271 (Alaska 1994).

This section applies to a clause that is questioned under this statute regardless of whether indemnification has been sought. City of Dillingham v. CH2M Hill N.W., Inc., 873 P.2d 1271 (Alaska 1994).

Section applicable to equipment leases. — This section should be applied to void indemnity clauses in equipment lease agreements if such a legal rule would advance the purposes of the anti-indemnity statute by inducing careful inspection and use of the leased equipment. Aetna Cas. & Sur. Co. v. Marion Equip. Co., 894 P.2d 664 (Alaska 1995).

When state is solely negligent. — This section should come into effect only when it is determined, as between the state and contractors, that the state is solely negligent. Rogers & Babler v. State, 713 P.2d 795 (Alaska 1986).

"Wilful misconduct" does not require intent to harm. — Wilful misconduct means volitional action taken either with a knowledge that serious injury to another will possibly result, or with wanton and reckless disregard of the possible results. Aetna Cas. & Sur. Co. v. Marion Equip. Co., 894 P.2d 664 (Alaska 1995).

Because the insured was found by a jury to have acted with reckless disregard of the plaintiff's interests and safety, the insured's injurious behavior is properly termed wilful misconduct. Consequently, this section forbids the indemnity the insurer seeks. Aetna Cas. & Sur. Co. v. Marion Equip. Co., 894 P.2d 664 (Alaska 1995).