

Oregon  
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Seminars

# Insights into Indemnification Provisions



*Cosponsored by the Business Law Section*

**Thursday, July 16, 2015**  
**8 a.m.–9:30 a.m.**

**1.5 General CLE credits**

# INSIGHTS INTO INDEMNIFICATION PROVISIONS

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## FACULTY

**Jeffrey Cronn**, *Tonkon Torp LLP, Portland*. Mr. Cronn is cochair of Tonkon Torp's Business Department and an active member of the firm's Corporate Finance and Nonprofit practice groups. His practice emphasizes mergers and acquisitions and a range of corporate and business matters. He regularly counsels public, private, and nonprofit entities with respect to mergers and acquisitions, corporate governance, securities and financings, and other general corporate matters and also advises clients with regard to equity ownership disputes. Mr. Cronn is a member of the American Bar Association and Multnomah Bar Association. He is the coauthor of the chapter on financing for *Advising Oregon Businesses* (Oregon CLE 2001 & Supp 2007). Mr. Cronn is a frequent speaker before industry and professional groups on M&A, finance, and corporate governance issues.

**Darren Nakata**, *Perkins Coie LLP, Portland*. Mr. Nakata's practice focuses on strategic corporate transactions and advice, including mergers and acquisitions, private and public debt and equity financings, joint ventures and other strategic partnerships, and corporate governance matters. He began his legal career in New York City, where he represented buyers and sellers in M&A transactions, lenders/underwriters and borrowers/issuers in complex leveraged and acquisition finance transactions, private equity firms and their portfolio companies in a wide range of transactions, and a variety of global companies in complex cross-border transactions.

**Jeremy Sacks**, *Stoel Rives LLP, Portland*. Mr. Sacks is a partner in the firm's Litigation Practice Group, chair of the firm's Energy Litigation Initiative, and chair of the Portland office trial group. His practice focuses on complex litigation in a variety of businesses, including the energy industry. He has experience litigating business torts, contract disputes, securities fraud, False Claims Act issues, shareholder disputes, class actions, licensing disputes, and antitrust claims. Mr. Sacks also has substantial experience conducting internal corporate investigations and handling export and import matters. He has represented individual and corporate clients, both regional and national, in a variety of private, state, and federal forums. Mr. Sacks is a member of the American Bar Association Litigation and Antitrust sections and the Multnomah Bar Association. Mr. Sacks is admitted to practice in Oregon, Washington, California, and the District of Columbia, as well as before the U.S. Court of Federal Claims and the U.S. Court of International Trade.



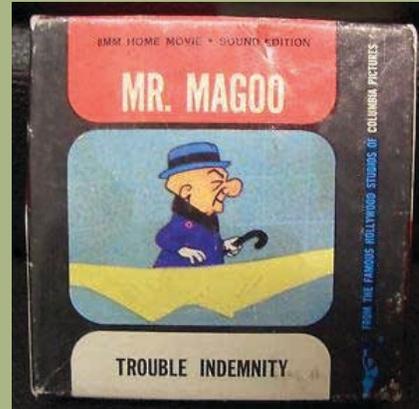
## Chapter 1

# Trouble Indemnity—Presentation Slides

JEFFREY CRONN  
Tonkon Torp LLP  
Portland, Oregon



## Trouble Indemnity



### Oregon State Bar Indemnification Provisions

Jeffrey S. Cronn  
July 16, 2015



## Limits and Exclusivity of Indemnity Remedies

- Special indemnities
  - Tax, environmental, ERISA
  - Undisclosed Liabilities
  - Diligence issues (IP, product liability, pending claims, etc.)
- Exclusivity of indemnity as a remedy
  - In 94% of 2012 deals (silent in another 4%)
  - Typical carve-outs:
    - Intentional misrepresentation (25% in 2012)
    - Equitable remedies (64% in 2012)
    - Breach of covenant (13% in 2012)
    - Fraud (82% in 2012)



## Fraud Exception

- Defined? (“actual fraud,” “intentional fraud,” “fraud or intentional misrepresentation”)
  - Not defined in 81% of deals in 2012
- 10b-5
  - No untrue statement of material fact or omission of material fact (ABA Model SPA)
  - Not in 64% of deals in 2012
- Full Disclosure
  - No Knowledge of any fact \* \* \* that may materially adversely affect the assets, business, prospects, financial condition or results of operations of Seller (ABA Model APA)



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## Third-Party Claims

- Right to assume defense of a third-party claim
  - Claims notice / notice procedure
  - Consequences of delinquent notice
  - Selection of counsel
  - Right to negotiate, litigate, settle
- Limit attorney fees
- Subrogation



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## Claims Among Indemnifying Parties

- Contribution
  - Many flavors
    - Joint and several
    - Capped joint and several
    - Several
    - Joint and several for some, several for others
- Contribution Agreements
- Structure of obligations depends on payors
  - Who can pay?
  - Don't want to chase many small holders
  - Small holders won't agree to be on the hook for everything

## Hidden Issues: Drafter Beware

- Importance of Drafting Detail
  - Special indemnities
    - May subsume specific indemnities
    - May prolong indemnity period
  - General provisions may defeat specific indemnities
  - The Double Dip: A working capital true-up coupled with an indemnity claim
- Bait and Switch
- Law may restrict indemnity remedy (and vice versa)

## Sample Provisions

- *Carve Out for Undisclosed Liabilities:* Any liability of the Company or any Subsidiary existing on the Closing Date other than (i) Liabilities set forth on the Most Recent Balance Sheet, (ii) Liabilities which have arisen since the Most Recent Balance Sheet Date in the Ordinary Course of Business, (iii) contractual and other Liabilities incurred in the Ordinary Course of Business which are not required by GAAP to be reflected on a balance sheet and that are not in the aggregate material, and (iv) Liabilities set forth in Schedule \_\_\_\_\_ of the Disclosure Schedule.



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## Sample Provisions

- *Exclusivity of Indemnity:* Except for any injunctive relief to which a Party may be entitled, the indemnification remedies provided in this [Article] shall constitute the exclusive remedy of the parties after the Closing for any claim for breach of any representation or warranty made in connection with this Agreement. The limitations of this Section...shall not apply to claims based on fraud.



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## Sample Provisions

- *Contribution:* References in this Agreement to "Joint and Several" or "Jointly and Severally" shall mean that the Parent, [Party] and the Parent Indemnitees, as applicable, shall be entitled to recover any and all relevant Damages on a joint and several basis from [certain named shareholders] (such Shareholders, the "**Joint Shareholders**") and from all other Shareholders (the "**Non-Joint Shareholders**"), provided that the amount that Parent, [Party] and the Parent Indemnitees shall be entitled to recover from a Non-Joint Shareholder shall be limited to that Non-Joint Shareholder's Pro Rata Portion of the Damages in question.



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## Sample Provisions

- *Third Party Claim:* If Indemnitor elects to assume responsibility for the defense and resolution of the Third Party Claim as permitted herein...Indemnitor will have the right to settle the Third Party Claim as follows:
  - Indemnitor may settle the Third Party Claim without Indemnitee's consent if the settlement will not create any Liability or other obligation on the part of Indemnitee that is not paid, satisfied or discharged by Indemnitor and unconditionally releases Indemnitee from all Liability in connection with the Third Party Claim.
  - Indemnitor may not settle the Third Party Claim without Indemnitee's prior written consent if the settlement does not meet the description set forth in [the section above], which consent may be granted or withheld in Indemnitee's discretion. Unless the required consent is obtained, Indemnitor will continue to defend the Third Party Claim.
  - Indemnitor will have no liability with respect to any compromise or settlement of the Third Party Claim effected without Indemnitor's consent, which may not be unreasonably withheld.



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## Chapter 2

# Indemnification Provisions—Presentation Slides

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PERKINScoie  
COUNSEL TO GREAT COMPANIES

Oregon State Bar

# Indemnification Provisions

CLE Presentation

Darren Nakata  
July 16, 2015

Perkins Coie LLP

## Representations & Warranties

**“Standard” representations and warranties vs. “Fundamental” representations and warranties**

- Organization, authority, capitalization
- Taxes
- Employee benefits, environmental
- Intellectual property
- Brokers
- Others on a deal-specific basis

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## Covenants & Limitations

### Covenants and other obligations

#### Limitations

- Survival periods
- Basket
  - Deductible vs. dollar one/tipping basket
  - Mini-basket
  - Hybrid
- Cap

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## Material Breach & Damages

### Materiality scrapes (for breach, for damages)

- Cancel “layering” effect of materiality (basket, mini-basket)
- Efficiency – negotiation of materiality qualifiers; what constitutes materiality in post-closing disputes
- Increasing size of basket or mini-basket; excluding certain representations and warranties from scrape

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## Sandbagging & Anti-Sandbagging

### Sandbagging, anti-sandbagging

- Right to close and pursue claim during post-closing period despite knowledge of pre-closing breach by other party
  - Disputes about knowledge
  - Role of proper diligence
  - Use of disclosure schedules
- Preclude post-closing claims for issues that “arose” during diligence
  - Close and sue
  - Diligence and use of disclosure schedules and special indemnities

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## Indemnities & Provisions

### Setoff provisions

- Indemnification
- Holdback
- Earnout

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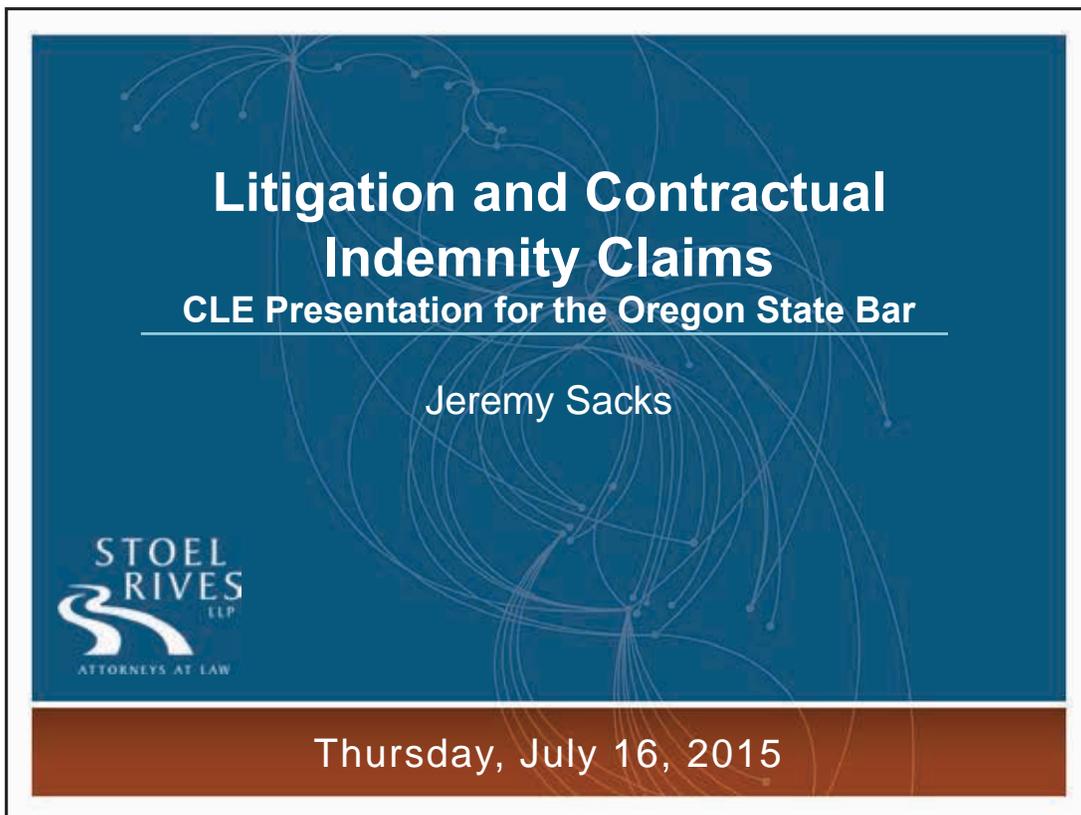


## Chapter 3

# Litigation and Contractual Indemnity Claims—Presentation Slides

JEREMY SACKS  
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Portland, Oregon



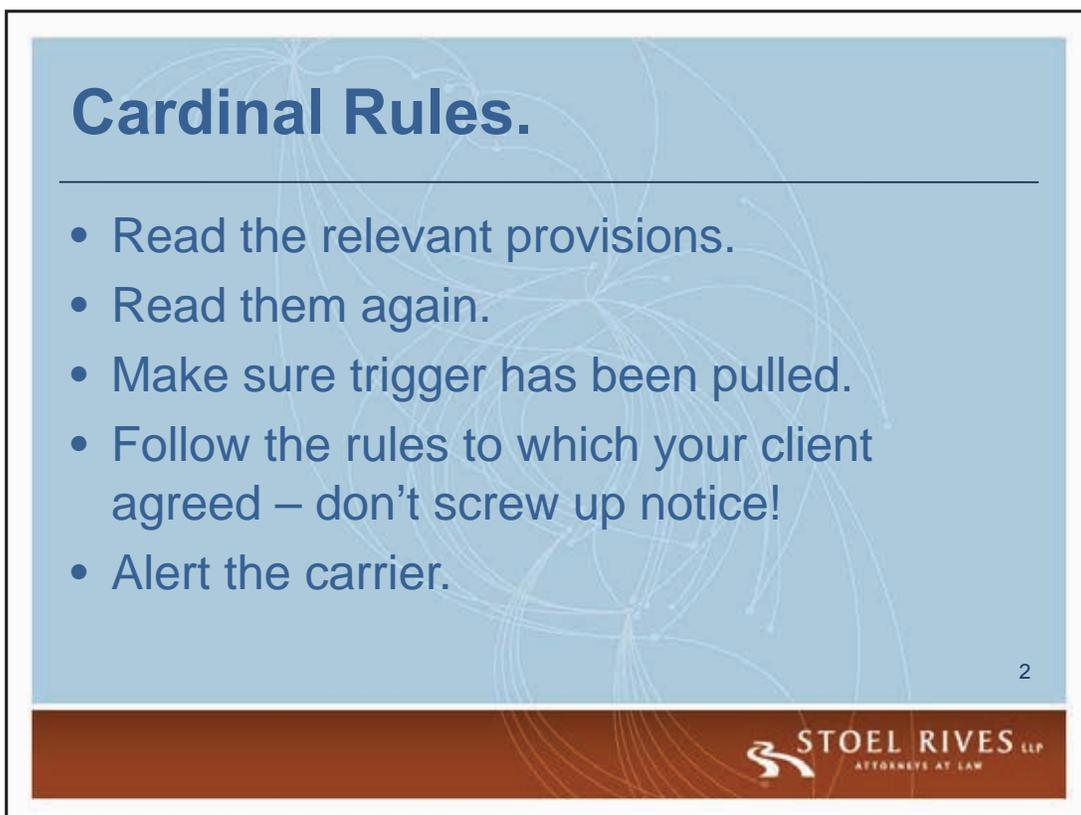


**Litigation and Contractual  
Indemnity Claims**  
CLE Presentation for the Oregon State Bar

Jeremy Sacks

**STOEL RIVES  
LLP**  
ATTORNEYS AT LAW

Thursday, July 16, 2015



**Cardinal Rules.**

- Read the relevant provisions.
- Read them again.
- Make sure trigger has been pulled.
- Follow the rules to which your client agreed – don't screw up notice!
- Alert the carrier.

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**STOEL RIVES  
LLP**  
ATTORNEYS AT LAW

## Types of Indemnification.

- Contractual indemnity.
  - Indemnification for *direct breach of reps and warranties* by other party to contract.
  - Indemnification for claims by third party based on breach of reps or warranties or identified source of potential losses.

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## Types of Indemnification.

- Common law indemnity.
  - Fills gap where there is no contractual indemnity provision.
  - *Eclectic Inv., LLC v. Patterson*, 357 Or. 25 (2015): No common law indemnity rights in cases where jury will be asked to allocate fault (*i.e.*, negligence, gross negligence, strict liability).

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## Scope of Indemnity.

- Does it cover only losses? Or does it also include attorney fees and costs of defense against claim that triggered indemnity.
  - Direct claim against other party to contract?
  - Third party claim?
  - Look to the language of the provision.

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## Indemnity and Claim Defense.

- Duty to Indemnify  $\neq$  Duty to Defend.
  - Duty to Indemnify: Protect indemnitee from a covered loss corresponding to the injury itself; depends on the outcome of the claim.
  - Duty to Defend: Provide defense of a covered claim; does *not* depend on the outcome of the claim.

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## Hold Harmless Clause.

- In Oregon, a hold harmless clause generally is interpreted as a duty to defend (or to reimburse defense costs).
- *Sunset Presbyterian Church v. Andersen Constr. Co.*, 309 Or. 310, 315 (Or. App. 2014).

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## Defense of Third Party Claim.

- When there is a duty to defend, usually:
  - Indemnitee must provide “reasonable assistance” to indemnitor, at indemnitor’s expense, in defending claims.
  - Indemnitee has the right to control defense of claim or suit filed against it at indemnitee’s expense.

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## Conflicts and the Duty to Defend.

- If the indemnitor and indemnitee have a legal conflict, does the indemnitor have to pay for the costs of the litigation and allow the indemnitee to control the defense under Oregon law?
  - Probably not, outside environmental arena.
  - Similar cases in the insurer/insured context indicate the insured does *not* have a right to control its own defense when insurer is paying for legal fees/costs under a reservation of rights.

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## Conflicts and the Duty to Defend.

- Relevant Oregon cases: *Ferguson v. Birmingham Fire Ins. Co.*; *Farris v. USFG.*
- OSB Formal Opinion 2004-121: lawyer retained by insurer to represent insurer and insured must treat insured as primary client. See *also* Rule 1.8(f).
- Environmental cases: ORS 465.483 establishes right to independent counsel.

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## Conflicts and the Duty to Defend.

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- Privilege issues.
  - If one attorney represents both the indemnitee and indemnitor:
    - Conversations between the attorney and either or both clients are privileged as to third parties; work product protection applies as to third parties as well.

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## Conflicts and the Duty to Defend.

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- Privilege issues.
  - If one attorney represents both the indemnitee and indemnitor:
    - As between the two clients, what one client shares with the lawyer is *not* privileged vis-à-vis the other client.
    - In a subsequent action between the two clients, there is no privilege as to the communications already shared.
    - OEC 503(4)(3).

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## Conflicts and the Duty to Defend.

- California rule is the opposite: Where there is a conflict, indemnifying party cannot control defense of indemnified party or require indemnified party to pay for its own defense. See *San Diego Fed. Credit Union v. Cumis Ins. Soc'y*; Cal. Civ. Code § 2778(4); *Safeway Stores, Inc. v. Mass. Bonding & Ins. Co.* (all ins. context).

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## Forum for Dispute over Indemnity.

- Choose a court.
  - Judges and juries generally get it right.
  - If they don't you can appeal.
  - Built-in procedures to resolve dispute early (MTD, MSJ, etc.).
- Arbitration is not a silver bullet.
  - Can be as expensive as trial and no appeal rights; prone to splitting the baby.

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