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STATE OF NORTH DAKOTA

IN THE SUPREME COURT

FOR THE STATE OF NORTH DAKOTA

Specialized Contracting, Inc., a North Dakota corporation, Plaintiff, vs. St. Paul Fire & Marine Ins. Company, a foreign insurance company, Defendant and Third Party Plaintiff, vs. City of Valley City, a municipal corporation, Third Party Defendant and Third Party Plaintiff / Appellee, vs. Geo. E. Haggart, Inc., a North Dakota Corporation, Third Party Defendant, and Kadrmas, Lee & Jackson, Inc., a North Dakota corporation, Third Party Defendant / Appellant.	**Supreme Court No. 20120195** Barnes County District Court No. 02-07-C-00258

BRIEF OF APPELLANT

APPEAL FROM THE JUDGMENT ON THIRD PARTY DEFENDANT AND THIRD PARTY PLAINTIFF CITY OF VALLEY CITY'S DUTY TO DEFEND CLAIMS AGAINST THIRD PARTY DEFENDANTS GEO. E. HAGGART, INC., AND KADRMAS, LEE & JACKSON, INC. DATED APRIL 5, 2012 IN THE BARNES COUNTY DISTRICT COURT, SOUTHEAST JUDICIAL DISTRICT

THE HONORABLE JAY A. SCHMITZ, PRESIDING

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¶3 **STATEMENT OF THE ISSUES**

¶4 1. Did the trial court err in not dismissing Kadrmas, Lee & Jackson from the trial of this matter?

¶5 Answer: Yes.

¶6 2. Are the indemnity provisions indemnification against claims only and not indemnification against liability?

¶7 Answer: Yes.

¶8 3. Is KLJ entitled to recover its costs and disbursements?

Answer: Yes.

¶9 **STATEMENT OF THE CASE**

¶10 Specialized brought suit against the bonding company, St. Paul for recovery of its additional costs. St. Paul, filed a Third Party Complaint against the City contending that if Specialized is able to establish that it was denied payment for labor and material it was ordered to perform outside the scope of the contract, that the City would be liable to Haggart for that payment and further, should Specialized establish that its work on the project was delayed because of work that it was ordered to perform outside the scope of the contract, then the City would be liable to Haggart for the liquidated damages assessed and withheld.

¶11 The City filed a Third Party Complaint against Haggart and KLJ contending that KLJ has a duty to defend and indemnify the City for any liability arising out of the Plaintiff's Complaint and the Third Party Complaint of St. Paul. The Third Party Complaint against KLJ alleges that the damages of Specialized and/or St. Paul were the direct and proximate result of the acts, omissions, fault, negligence, malpractice, breach of contract, breach of warranty or conduct and/or omissions of KLJ and others under their direction, supervision and control. The case was tried to a jury on March 15-19, 2010. The jury returned a verdict dismissing the Plaintiff's Complaint.

¶12 After trial, the City of Valley City requested attorney's fees and costs pursuant to an indemnity provision in the contract between the parties. This was granted by the court.

¶13 KLJ appeals from the denial of the Motion for Summary Judgment and from the Order requiring KLJ to indemnify the City for its costs.

¶14 The appeal in this case is important, not because of the dollar amount involved, but because of the impact of the ruling on many design professional contracts in existence in the

State of North Dakota. Custom and usage with regard to the provision involved in the contract between the parties has been to treat this provision as a contract of indemnity against claims made, not an indemnity against liability. The ruling of the trial court significantly shifts the risks and costs to the design professional contrary to custom and practice. Also, the fees and costs incurred by KLJ by force to remain in this suit and defend at trial sets an extremely bad precedent.

¶15 **STATEMENT OF THE FACTS**

¶16 On April 22, 2005, Geo. E. Haggart, Inc. ("Haggart") entered into a Contract with the City of Valley City ("City") to furnish labor, materials and equipment required for the paving and construction of Fifth Avenue NE, known as Project No. SU-TEU-2-990(018)023. St. Paul Fire & Marine Insurance Company ("St. Paul") and Haggart executed the bond for the project.

¶17 Haggart entered into a subcontract with Specialized Contracting, Inc. ("Specialized") to provide the labor and materials for certain portions of the project including the concrete paving and curb and gutter work.

¶18 Kadrmas, Lee & Jackson ("KLJ") was the project engineer and prepared drawings, plans and specifications. The plans incorporated the North Dakota Department of Transportation's Standard Specifications for Road and Bridge Construction (2002) ("NDDOT Specifications").

¶19 The work done by Specialized on the project resulted in cracking and they were required to remove and replace the concrete. Specialized claims it was due compensation for this. Specialized also sought reimbursement for removal and replacement of concrete in the south intersection of the project. This was necessary to correct the drainage problem resulting from the original work. Specialized also claims damages for additional costs incurred, retainage and liquidated damages that were imposed. Specialized filed claims for recovery of the additional compensation and they were denied.

¶20 On September 24, 2007, Haggart signed the Final Claim for Payment certifying that the amount stated was full and final payment on the contract for the project.

¶21 **ARGUMENT**

¶22 **I. THE COURT ERRED IN NOT DISMISSING KLJ FROM THE CASE.**

¶23 **A. Haggart released the City from liability.**

¶24 As shown in the attachment to the Affidavit of Leslie S. Norton (App. p. 42) filed in support of KLJ's Motion for Summary Judgment, Haggart released the City from any liability by certifying that it had been paid in full and final payment on the contract for the project. *See also* VC Exhibit 551. As a matter of law, the claims against the City should have been dismissed prior to trial. Because the City had no liability, its Third Party Complaint for indemnification against KLJ should have been dismissed.

¶25 N.D. Cent. Code § 24-02-25.1 establishes when a claim may be filed against a project. The statute provides that any person who has furnished labor and materials and has not been paid in full at the time of final acceptance, has the right to file a claim against the contractor and the surety. In this particular case, this means Specialized had the right to sue Haggart or its bonding company. There is nothing in this statute that permits a claim against the owner or the design engineer after full and final payment has been made on the contract.

¶26 Paragraph 104.06.B of the NDDOT Specifications governing this project states that:

> "If the Contractor signs the final payment voucher and certifies that the quantities are a true and correct statement of the work performed, the Contractor, by his action, accepts the amount stated as full and final payment on the Contract for the stated Project and waives all rights to any additional payments to complete the Project."

¶27 NDDOT Specifications apply to this case because the project was partially federally funded and NDDOT administers a portion of the funding, with the City agreeing to follow NDDOT regulations through the NDDOT Urban Roads Program. Specialized had the right

to bring an action against Haggart and St. Paul. No action should have been permitted against the City, and therefore KLJ, because Haggart had signed and confirmed that it has been paid in full. Even if Specialized could have established the right to recover from Haggart, Haggart was barred from filing any claim against the City. This cannot be circumvented by having St. Paul file the claim on behalf of Haggart.

¶28 For these reasons, the Third Party Complaint against the City of Valley City should have been dismissed prior to trial as should the Third Party Complaint by the City against KLJ.

¶29 **B. KLJ did not breach any duty.**

¶30 In a negligence action, the plaintiff [the City] must prove (1) duty; (2) breach of that duty; (3) causation; and (4) damages. Miller v. Diamond Resources, Inc., 2005 ND 150, ¶ 10, 703 N.W.2d 316; Investors Real Estate Trust Properties v. Terra Pacific Midwest, 2004 ND 167, ¶ 7, 686 N.W.2d 140 (*citing* Barbie v. Minko Construction, Inc., 2009 ND 99, ¶ 8, 766 N.W.2d 458).

¶31 There was no evidence that any employee or representative of Kadrmas, Lee & Jackson was in any way negligent or breached its duty of care to the City. Prior to trial, KLJ brought a Motion for Summary Judgment because the City had not disclosed any expert who would testify that KLJ breached its standard of care. The trial judge denied this motion.

¶32 The trial judge disclosed his reasoning at different stages of the trial. The reasoning has no legal basis, it is just the judge's preference:

> "And not necessarily to show my hand, but I think it's important that all four of these parties remain in this trial because I've always had this concern, and I've told you this before, I've always had this concern that if it was just

Specialized and St. Paul and Haggart that we could go through this five day trial and the jury would say well, we think the real person who is liable here is the City because they shouldn't have done this. Or the real person who is liable is KLJ because they shouldn't have recommended that to the City. And it's a waste of time in my mind if the jury on that 5th day says if KLJ and the City were out of the case, it would be a waste of time if they're going to say well, we think it's the City and the engineer who are responsible, but then they're out of the case. And then you have to start all over again." Tr. p. 528.

"Well, I think it's safe to say that we don't have much or perhaps any evidence of the type of negligence you would expect in a negligence action. What I'm talking about is a breach of duty at the scene. And I haven't heard anything necessarily that KLJ did a poor job of supervising construction, they did a poor job of planning. There's some evidence about the staking, and that's in dispute about how those stakes happened to change. And I think that's a fact question for the jury. That could be negligence perhaps, but there isn't much of that.

Now on this other issue about KLJ making a decision between two types of remedies, you can -- I think that's a fact issue for the jury. And I'm sure that that was going to be argued heatedly. And that is that KLJ could look at this and say well, the one solution that would work just fine is where we go and we route and we clean and we fill these cracks, but they chose the second option. They said no, make them tear it up and re-pour it. Do it over again. And that's the option that was followed by the City of Valley City. That could -- They could make the argument to the jury that that's some type of professional negligence when they're clearly in black and white whether or not there was another viable option that they could have used. So I'll deny the motion." Tr. p. 689-690.

¶33 This is not a case where the court had to weigh evidence regarding potential negligence of Kadrmas, Lee & Jackson. The court was not required to do an extensive review of any statute, rule or regulation, or the plans and specifications. The simple fact is that there was **no evidence** of any kind upon which a claim of negligence could be based. The Complaint as against KLJ should have been dismissed.

¶34 Prior to trial, the City addressed claims that may arise with respect to attorney's fees.

The suggestion of the City was that subsequent to trial the issue would be submitted for consideration by the Court if a determination was made that KLJ must indemnify the City against liability. Tr. p. 26-27. With removal, however, of the question of legal fees from the jury trial, the only issue that remained against KLJ was the claim of the City that KLJ was negligent. None of the parties attempted to prove that KLJ was negligent. Mr. Nodzon, on behalf of Specialized Contracting, Inc., in his opening argument, made it clear that Specialized had no claims against KLJ. Tr. p. 168, l. 18-21.

¶35 The court, in its opening instructions to the jury, informs the jury that "the City of Valley City sued Geo. E. Haggart, Inc., and KLJ, seeking reimbursement for any damages that the City pays to St. Paul Fire & Marine." There is no statement about negligence. Counsel for the parties made no objections to this instruction.

¶36 Douglas Gigler, in his opening argument on behalf of St. Paul Fire & Marine and Geo. Haggart, stated, "We think the evidence is going to show that KLJ was entirely justified in making that decision." Tr. p. 197, l. 17-19. He later states, "and its specifications allowed KLJ to reject that work and order SCI to remove it and replace it at SCI's expense." Tr. p. 198, l. 23-25. Later, in his opening argument he states, "... but at the same time we think that the evidence is going to show that even though the City is in this case based on KLJ's decisions, those decisions were sound, supported by the evidence, and supported by the law, and the plans and specifications of this project." Tr. p. 203, l. 5-10.

¶37 Daniel L. Gaustad, speaking for the City of Valley City, in his opening argument stated, "The decisions made by KLJ during the construction were justified." Tr. p. 207, l. 5-6. "KLJ did all the Plan and Specs. They made appropriate proper decisions." Tr. p. 208, l.

12-13. "But from Valley City's standpoint, the evidence is going to show that the decisions by KLJ to reject and make SCI do the work so that Valley City got the product it was entitled and paid for were proper and justified." Tr. p. 209, l. 6-10.

¶38 There was no virtually no evidence of negligence presented throughout the trial. In fact, the Mayor of Valley City testified as follows:

> QUESTION: (By MR. MAUS) So wouldn't it be true that KLJ was actually doing their job properly and advising the City don't accept an inferior product?
>
> A. That would be true.
>
> Q. And, in fact, you personally don't believe that KLJ committed any negligence on this job, do you?
>
> A. No, I do not.

Tr. p. 682, l. 13-20.

¶39 KLJ should not have been a participant in the trial. KLJ's Motion for Summary Judgment should have been granted. The negligence claims were at best frivolous and for the sole purpose of forcing KLJ to incur unnecessary expense. The result was that one of the vice presidents of the company and two of the employees sat through a four-day trial. The company spent in excess of $40,000 for legal fees and expert witnesses' fees that were not necessary if the only issue that remained was one that would be decided by the court **after the trial**.

¶40 The issues that were actually presented to the jury involved reimbursement arising from the decision by KLJ to recommend to the City that they require the contractor to remove certain concrete that had cracked. The City followed the recommendation of KLJ and the

concrete was removed and replaced. The question before the jury was whether requiring removal of the concrete was consistent with the plans and specifications that applied to the job, or whether Specialized should have been allowed to patch and repair.

¶41 The second major issue was the recommendation of KLJ to require the contractor to take out and replace an intersection because after completion it did not drain properly. These issues did not deal with negligence by KLJ.

¶42 There were separate issues of Specialized Contracting against St. Paul Fire & Marine and Geo. E. Haggart, Inc., dealing with payment for manholes, retainage and liquidated damages. None of these issues have anything to do with KLJ and are not part of this appeal.

¶43 The evidence presented to the jury showed that the cracking in the concrete was a result of not sawing the joints at the proper time and the wrong aggregate mix, both of which are within the means and methods of the contractor. There was no evidence of any negligence by KLJ.

¶44 There were no complaints made about the work of KLJ in designing the plans and specifications. There is no evidence that KLJ breached any duty in designing this project or as project engineer. KLJ's Motion for Summary Judgment should have been granted and they should not have been required to participate in the trial.

¶45 C. KLJ was entitled to summary judgment because the City did not retain an expert to establish professional negligence.

¶46 The City should have been required to produce expert testimony because the issue of professional negligence is "beyond the area of common knowledge or lay comprehension." Leno v. Ehli, 339 N.W.2d 92, 99 (N.D. 1983).

¶47 Generally, expert testimony is necessary to establish the professional standard of care (duty) and whether the professional's conduct in the particular case deviated from that standard of care (breach of duty). Sheets v. Letnes, Marshall & Fiedler, Ltd., 311 N.W.2d 175 (N.D. 1981); Winkjer v. Herr, 277 N.W.2d 579 (N.D. 1979). There is an exception when the professional's misconduct is so egregious and obvious that a layperson can comprehend professional's breach of duty without the assistance of expert testimony. *See* Carlson v. Morton, 229 Mont. 324, 745 P.2d 1133 (Mont. 1987); Winkjer v. Herr, *supra*. That was not the case in this lawsuit. Because of the complexities of engineering design, expert testimony would be required to establish the professional standard of care and a breach of that duty.

¶48 It could not reasonably be argued that the causal relationship between the engineering work and the claim of Specialized is a matter within the common knowledge or comprehension of a layperson. As stated by the Supreme Court in Johansen v. Anderson, 555 N.W.2d 588 (N.D. 1996):

> Unlike professional malpractice actions, there is no requirement in ordinary negligence cases for expert testimony to establish the standard of care and whether the defendant's professional conduct deviated from that standard.

¶49 The allegations of the City in this case against KLJ included claims of professional malpractice. Accordingly, there was a requirement for expert testimony to establish the standard of care and a breach of that care. *See also* Richmond v. Nodland, 501 N.W.2d 759 (N.D. 1993); Wastvedt v. Vaaler, 430 N.W.2d 561, 565 (N.D. 1988).

¶50 In other jurisdictions, expert testimony has been required to establish engineering malpractice. One such case is Peck v. Horrocks Engineers, Inc., 106 F.3d 949 (10th Cir.

1997). In that case, Peck produced no expert testimony from which a jury could infer Horrocks engineering malpractice. The court stated, "whether or not the [engineer] exercised proper or reasonable judgment would have to be based upon the testimony of other [engineers] and not upon the testimony of lay persons, ..." *Quoting* Nauman, 567 P.2d at 615. The case was dismissed as against Peck because he produced no expert testimony that the engineers acted unreasonably or in a negligent fashion.

¶51 A similar case is Gibbes, Inc. v. Law Engineering, Inc., 960 F.2d 146 (4th Cir. 1992), where the court held that to establish professional negligence under Georgia law, Gibbes, Inc., was required to offer competent and expert testimony as to the standard of care applicable to an engineer performing a pre-construction geotechnical exploration. In that case, the court granted summary judgment for the defendant on the professional negligence and warranty claims.

¶52 The fact that there are multiple parties makes it even more necessary to produce expert testimony regarding the alleged negligence of KLJ. The case of Samson v. Riesing, 215 N.W.2d 662 (Wis. 1974), points out the importance of an expert specifically when there are multiple parties to address the need to prove specifically what a defendant did that was negligent. In Samson, the plaintiff attempted to prove circumstantially that someone was negligent. The plaintiff, however, failed to prove that a particular defendant failed to conform to the standard of care.

¶53 For these reasons, the City's Complaint of negligence as against KLJ should have been dismissed prior to trial, saving KLJ considerable time and expense. Because design professionals are often brought into lawsuits, it is important that the Court clarify this area

of the law.

¶54 **D. KLJ was entitled to summary judgment because the statute of limitations had expired.**

¶55 The Third Party Complaint of the City against KLJ alleged professional malpractice. The Complaint is dated May 28, 2009. The statute of limitations on malpractice is two years. N.D. Cent. Code § 28-01-18(3).

¶56 A Notice of Intent to File a Claim for "cracking" was submitted by Haggart to KLJ on September 7, 2005. The claim was received on April 11, 2006. KLJ responded to the claim on May 8, 2006. A Notice of Intent to File a Claim for removal and replacement of the intersection was submitted to KLJ on May 10, 2006. KLJ responded to this on June 7, 2006. No formal claim was ever filed on this. *See* Affidavit of Leslie Norton (App. p. 40). The City was aware of these claims and denied them.

¶57 Obviously, the work of KLJ that is claimed to be negligent occurred prior to the date of these claims. For these reasons, the Complaint of the City as against KLJ for professional negligence should have been dismissed.

¶58 The trial court ruled that the claim by Valley City was not barred by the two-year statute of limitations because it was not discovered until April 2009. The discovery rule is an exception to the limitations and, if applicable, determines when the claim accrues for the purposes of computing limitations. The discovery rule postpones a claim's accrual until the plaintiff knew, or with the exercise of reasonable diligence should have known, of the wrongful act and its resulting injury. Wells v. First American Bank West, 1999 ND 170, 598

N.W.2d 834. Courts generally apply the discovery rule when it would have been difficult for the plaintiff to have learned of the negligent act or omission that gave rise to the legal injury. Bates v. Texas State Technical College, 983 S.W.2d 821, 828 (Tex.Ct.App. 1998) (*citing* Computer Assoc. Int'l, Inc. v. Altai, Inc., 918 S.W.2d 453, 456 (Tex. 1996)). The North Dakota Supreme Court has used an objective standard for the knowledge requirement under the discovery rule. BASF Corp. v. Symington, 512 N.W.2d 692, 695 (N.D. 1994). The focus is upon whether the plaintiff is aware of facts that would place a reasonable person on notice a potential claim exists, without regard to the plaintiff's subjective beliefs. *Id.* (*citing* Biesterfeld v. Asbestos Corp. of America, 467 N.W.2d 730 (N.D. 1991).

¶59 The question is when the City should have discovered it had a potential claim against KLJ. The City became aware of the potential suit against KLJ when Specialized and Haggart filed the two separate Notices of Intent to File a Claim in 2006. No one disputes that the City had this knowledge.

¶60 In response to the Motion of KLJ to dismiss the Complaint because of the statute of limitations, the City relies on the fact that Haggart signed and delivered the final pay statement which released the City of Valley City. It argues that since it had not been sued and had been released by Haggart, that the knowledge of the claims filed was not sufficient to alert them of potential wrongful acts of KLJ. Belief in the legal implications of a document does not erase knowledge obtained prior to the existence of that document. Certainly a reasonable person would have wondered, when the claims were filed, whether KLJ had done everything properly. The rule cannot be that the statute of limitations only begins to run when you are sued. Nor can the rule be that if you think you have been released

and you have not actually been released, that the statute does not run.

¶61 Under the discovery rule, the statute commences to run when the plaintiff knows, or with reasonable diligence should know, of (1) the injury, (2) its cause, and (3) the defendant's possible negligence. Wahl v. Lewis, 393 N.W.2d 758, 761 (N.D. 1986). The City was aware of the injury, its cause and KLJ's possible negligence when Specialized/Haggart filed their Notices of Intent to File Claims. The fact that the City was not sued at that time does not change the knowledge that it had. The standard requires only that the plaintiff be aware of facts that would place a reasonable person on notice that a potential claim exists. Reimers v. Omdahl, 2004 ND 188, ¶ 6 and 7, 687 N.W.2d 445.

¶62 The fact that the City had not been sued or that Haggart had released the City does not change the knowledge which the City had of the "wrongful acts" of KLJ. Even after the suit was brought, the City did not really believe there were any wrongful acts by KLJ, but fabricated these allegations to force KLJ into the lawsuit.

¶63 Valley City's totally inconsistent position of following the recommendations of KLJ to have the concrete replaced and the intersection replaced, and espousing these as correct decisions, and its subsequent allegations that these decisions were negligent, should not have been permitted throughout the litigation. A party has to choose one position or the other, not try to benefit from alternating inconsistent positions.

¶64 This statute of limitation argument relates to the claims of professional negligence, not to the City's separate argument for indemnity which is a contract claim with a different statute of limitations.

¶65 **II. THE INDEMNITY PROVISIONS ARE PROVISIONS AGAINST**

CLAIMS MADE, NOT LIABILITY.

¶66 **A. <u>Interpretation of the Contract Provision</u>.**

¶67 KLJ entered into a contract with the City of Valley City. The contract contains an indemnification clause addressing professional services. This provision provides:

> **Indemnification for Professional Services:**
>
> The Professional (KLJ) agrees to indemnify, save, and hold harmless the Governments (City) from liability, including all costs, expenses, and reasonable attorney's fees, which may arise out of or result from the Professional's negligent acts or omissions in rendering professional services under this agreement. The Professional shall not be responsible for any amount disproportionate to the Professional's culpability. The additional-insured coverages and protections and indemnification provided elsewhere in this agreement shall not be limited or reduced by this paragraph.

This clause provides for indemnity against loss, not liability.

¶68 The North Dakota Century Code sets forth rules indicating when an indemnified person is entitled to recover:

> In the interpretation of a contract of indemnity, **unless a contrary intention appears**, the following rules are to be applied:
>
> 1. Upon an indemnity against liability, expressly or in other equivalent terms, the person indemnified is entitled to recover upon becoming liable.
>
> 2. Upon an indemnity against claims, demands, damages, or costs, expressly or in other equivalent terms, the person indemnified is not entitled to recover without payment therefor.
>
> 3. An indemnity against claims, demands, or liability, expressly or in other equivalent terms, embraces the costs of defense against such claims, demands, or liability incurred in good faith and in the exercise of reasonable discretion. ...

N.D. Cent. Code § 22-02-07, *emphasis supplied.* The important language in the statute is "unless a contrary intention appears." The indemnification provision in this case shows a

contrary intention to what is stated in the statute. The Court must first determine the intent of the parties from the contract provision, and not apply the statute if the intent can be determined from the contract provision.

¶69 The language of the provision in the contract at issue in the present case indicates that the parties intended indemnification against loss. The provision states, "The Professional shall not be responsible for any amount disproportionate to the Professional's culpability." These words must be given some effect. Since KLJ's culpability is zero, there is no indemnification.

¶70 Unfortunately, the statute itself provides little guidance as to how a court determines whether a particular provision indemnifies against liability versus indemnifying against loss, and there are very few North Dakota cases on point. The singular North Dakota case that is on point is from 1937, but it remains good law.

¶71 In Jones v. Grady, 66 N.D. 479, 266 N.W. 889 (1936), the Court observed the rule, now codified in N.D. Cent. Code § 22-02-07, that there are two types of indemnity agreements:

> There is a clear distinction between a contract to indemnify against damages and a contract to save harmless from (indemnify against) liability. In the former, the indemnified parties must suffer loss before suit may be brought. In the latter, suit may be brought the moment that the liability against which they are indemnified is established, though they have paid no money or suffered no pecuniary detriment by reason of such liability.

Id. at 892-893.

¶72 In the very recent case of Hausler v. Felton, No. 10-5131, 457 F.App'x 727, 2012 WL 120057 (10th Cir. Jan. 17, 2012), the federal court applied an Oklahoma statute similar in

language to the first two provisions of N.D. Cent. Code § 22-02-07, describing the two types of indemnity. In the case, the court set forth the basic rules of contract interpretation, according to which the court must give effect to the parties' mutual intent. In this case, it is clear the parties intended that KLJ would have indemnity obligations only in proportion to its professional culpability, which was none.

¶73 The Louisiana Supreme Court explained that the two types of contracts are sometimes referred to as "insurance against liability" as distinguished from "indemnity against loss":

> In legal parlance "liability insurance" is used in both a broad and a narrow sense. When the term is used in a broad sense it includes both contracts of indemnity against loss and contracts of insurance against liability. But when the term is used in a narrow sense it refers only to contracts of insurance against liability as opposed to contracts of indemnity against loss.
>
> Under a liability policy (in the narrow sense) the insurer is required to make payment although the insured has not yet suffered any loss, for by definition the purpose of the liability policy is to shield the insured from being required to make any payment on the claim for which he is liable. Under an indemnity contract, by way of contrast, the insurer is only required to indemnify or make whole the insured after he has sustained actual loss, meaning after the insured has paid or been compelled to make a payment, his action against the insurer then being to recover the amount of such loss by way of indemnity.
>
> The general distinction between the two kinds of insurance is that if the policy is one against liability, the coverage thereunder attaches when the liability attaches, regardless of actual loss at that time; but if the policy is one of indemnity only, an action against the insurer does not lie until an actual loss in the discharge of the liability is sustained by the insured.

Quinlan v. Liberty Bank & Trust Co., 575 So.2d 336, 348-49 (La. 1990, *on reh'g* (1991) (citations omitted). A review of the contract provisions in this case shows that the provision in the KLJ contract is one of indemnity, not liability.

¶74 As noted in these cases, a court when considering the scope of an indemnity clause will apply basic contract principles to give effect to the parties' intent. "When interpreting indemnity contracts, ... as with contracts generally, the cardinal rule is that the contract must be interpreted to give effect to the mutual intentions of the parties if it can be done consistently with legal principles." Hoge v. Burleigh County Water Mgmt. Dist., 311 N.W.2d 23, 27 (N.D. 1981). The trial court made no attempt to ascertain the parties' intent from the contract provision and went directly to the statute. When the parties' agreement has been reduced to writing, the court will ascertain the parties' intention from the writing alone, if at all possible. *Id.* at 27. Likewise, the Lindsey court applied the general contract-interpretation rules that the court looks to the contract as a whole, as well as the circumstances surrounding the contract to determine the intent of the parties. Lindsey v. Jewels by Park Lane, Inc., 305 F.3d 1087 (8th Cir. 2000).

¶75 The Risk Management Appendix to the agreement signed by KLJ sets forth the requirements for indemnification for professional services. KLJ agreed to defend against "any acts which may arise out of or result from the Professional's negligent acts or omissions in rendering professional services under this agreement." The Appendix is quite direct as to what triggers a duty to indemnify or defend. The argument that this implies a duty to defend ignores the very specific language of the provision. The acts have to be negligent. There is no terminology which states that the negligence need only be alleged. It has to be actual negligence. The jury did not find KLJ negligent. The City did not try to prove KLJ was negligent. The discussion of whether there is any doubt as to the interpretation is irrelevant. The provision activated upon a finding of negligence. Without a finding of negligence, there

can be no negligent acts, and the provision cannot be activated. The contract provision governs, not the statute.

¶76 In fact, there was no evidence introduced at trial upon which a jury could have found KLJ professionally negligent. Specialized Contracting did not have to prove negligence by KLJ and did not attempt to do so. Valley City did not introduce any evidence or expert opinion that KLJ was professionally negligent.

¶77 Nothing can change the underlying fact that the Risk Management Appendix clearly states that indemnification would only arise from negligent acts or omissions, of which there were none. The fact that the provision exists does not matter since it never actually activated.

¶78 The City contends that because negligence remained a recurring issue throughout the course of litigation, that should have activated the duty to defend provision. It was not a recurring issue because there was no evidence of negligence produced. The provisions of the Risk Management Appendix clearly states that the duty to defend relates to actions arising out of KLJ's negligence.

¶79 An analogy can be made to liability insurance. KLJ agreed to indemnify Valley City, but only if KLJ were found negligent. Without a finding of negligence, there can be no indemnification. The duty only exists if an injured plaintiff actually wins in court, or as the North Dakota Supreme Court has put it, "if the allegations of the claimant's complaint would support a recovery upon a risk covered by the insurer's policy, then the duty to defend is present." Kyllo v. Northland Chemical Co., 209 N.W.2d 629, 634 (N.D. 1973), *citing* Eichler Homes, Inc. v. Underwriters at Lloyd's, London, 238 Cal.App.2d 532, 538, 47

Cal.Rptr. 843, 847 (1965). There was no evidence of negligence by KLJ in this case. Although not a perfect analogy, the comparisons are there. Without a finding of negligence, the indemnification clause remains dormant.

¶80 To further support the argument the threshold for invoking the indemnity clause was never reached, we should consider the fact the jury ruled the plaintiff never satisfied its burden of proof in this case, essentially eliminating all other claims.

¶81 Everything returns to the initial Risk Management Assessment. It stated that KLJ was only required to indemnify Valley City if there were negligence. There was no negligence. There is no need to consider the statute because the parties' intent is set forth in the contract. This is not an indemnity against liability. KLJ was and continues to be under no duty to defend.

¶82 **B. <u>KLJ's liability was an issue of fact decided by the jury</u>.**

¶83 The issue of KLJ's contractual liability to Valley City was addressed on the Special Verdict Form, Questions 19 and 27. Questions 19 and 27 deal specifically with KLJ's contractual liability to Valley City. These Special Verdict questions were requested by Valley City to be submitted to the jury. These questions do not differentiate between indemnity for liability or liability for loss. The City also agreed with the Special Verdict Form which provided that if Question 1 is answered "No", the jury need not address the remaining questions.

¶84 If KLJ's contractual liability was a jury question, what right does the City have, post trial, to ask the judge to rule that KLJ had a duty to defend? How is it first a question, and then it is not? A determination of the amount of attorney's fees may be a question for the

court, but the City agreed, by submitting the questions to the jury, that the threshold obligation was one for the jury to decide. If the jury had answered yes, KLJ would not have been in a position to then ask the court to decide that they did not have liability. It is acknowledged that left for the court to decide would have been the amount of fees and costs had the jury ruled that KLJ had breached the contract.

¶85 In addition to the question of KLJ's contractual liability being in the Special Verdict form, arguments on this contractual liability were made to the jury by the City's attorney. The issue was put to the jury. The contracts between the City and KLJ were submitted as evidence to be considered by the jury. The only purpose for that was because of the indemnification language in the contracts. This issue of contractual liability has, therefore, been decided and should have been precluded from further consideration by the court under the principle of *res judicata.*

¶86 *Res judicata* is a procedural device which disallows rehearing of claims which have already been decided in order to promote finality of judgments and to avoid waste and delay. Riverwood Commercial Park. LLC v. Standard Oil Co., Inc., 2007 ND 36, ¶ 13, 729 N.W.2d 101. The jury returned a verdict in this case, which stated the plaintiff did not satisfy its burden of proof against one of the defendants. This issue of contractual liability was submitted to the jury at the request of the City. There was no finding by the jury of contractual liability by KLJ. It cannot thereafter ask the Court to decide an issue that was submitted to the jury.

¶87 The primary thrust of Valley City's argument is that, as the issue of KLJ's liability was never answered by the jury, the indemnity and duty to defend clauses are still active and

Valley City deserves compensation. The City agreed that the jury did not have to answer these questions if it answered No. 1 no. It waived any right to separately submit the question to the court.

¶88 In the comparable case of Praus v. Mack, the possibility for an indemnity claim was rendered moot after the jury determined the plaintiff was 60% negligent in causing his own death. Praus v. Mack, 2001 ND 80, ¶ 23, 626 N.W.2d 239. In this case, the jury found SCI failed to satisfy its burden of proof. The City agreed that if the jury made that decision, it did not need to decide Questions No. 19 and 27.

¶89 The argument that the claim of the City is barred is overwhelming. First, there is the Order of Judge Simonson dated March 2, 2010, on KLJ's Motion for Summary Judgment. Essentially, the court determined that the claims raised by the City were fact issues to be determined by the jury. That is the law in this case.

¶90 In addition, there's the fact that at the trial the City argued in its closing argument that KLJ was contractually liable to the City and introduced into evidence the two contracts with the indemnity language.

¶91 Finally, there is Special Verdict Form Question No. 19 which asked whether Valley City has met its burden to demonstrate that KLJ is liable to Valley City under the contracts and Question No. 27 which asks, "Has Valley City met its burden of proof to demonstrate that KLJ is liable to Valley City for indemnity?" These questions were submitted to the jury.

¶92 Valley City agreed that if Question No. 1 was answered "No", that the jury did not have to answer the remaining questions. Valley City cannot have a second bite at the apple

and claim that now the court can make that determination, asking the judge to award something that the jury did not.

¶93 **C. <u>Valley City is liable to KLJ for indemnification</u>.**

¶94 The Design Agreement between KLJ and the City of Valley City (VC Exhibit 506), specifically states as follows:

> Owner further agrees to indemnify and hold the Engineer harmless from any and all costs, liability, real or alleged, in connection with the performance of work on this project, excepting liability proximately arising from the sole negligence of the Engineer.

If the contract provision for Indemnification for Professional Services is indemnification against liability, then this paragraph establishes that Valley City is liable to KLJ for its defense costs in this action. The Court must consider the entire contract. Unlike the provision which Valley City is relying upon, this paragraph is not limited as to whether or not the City has been negligent.

¶95 Because the indemnity provisions relied upon by Valley City are conditioned upon negligence by KLJ, and because the indemnity provision relied upon by KLJ is not conditioned upon negligence, the correct result is that the City is required to indemnify KLJ for its defense costs in this matter.

¶96 **III. KLJ SHOULD RECOVER ITS COSTS.**

¶97 The general rule of law is that the prevailing party in litigation is entitled to recover its costs and expenses. In this case, the City sued KLJ for negligence. They did not recover anything. KLJ incurred extensive defense costs, including the hiring of two expert witnesses who were instrumental in the Defendants prevailing in this matter. By statute, KLJ is

entitled to recover its costs and disbursements incurred in this action.

¶98 If the Court determines that KLJ must indemnify Valley City for its liability, KLJ does not object to the amount determined by the trial court.

¶99 **CONCLUSION**

¶100 KLJ should have been dismissed from this lawsuit because there was no proof of negligence and because the statute of limitation had expired. KLJ should be awarded its legal fees, costs and disbursements. The indemnity provision in the contract should be declared by the Court to be one of loss, not liability and the money judgment vacated.

¶101 Respectfully submitted this 26th day of July, 2012.

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¶102 **CERTIFICATE OF SERVICE**

I hereby certify that on the 26th day of July, 2012, I served the foregoing **BRIEF OF APPELLANT** on the following by electronic mail transmission, per N.D. Sup. Ct. Administrative Order 14(D):

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¶103 **CERTIFICATE OF COMPLIANCE**

I, Michael J. Maus, attorney for the Appellant Kadrmas, Lee & Jackson, Inc., do certify that the above Brief complies with all type-volume limitations as set forth in the North Dakota Rules of Appellate Procedure.

I further certify that the attached Brief of Appellant contains the following number of words: 6971 (excluding Table of Contents and Table of Authorities), and was prepared using WordPerfect X3, Times New Roman Font, Size12.

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