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Obtaining Indemnity Through Effective Tender Letters

Law360, New York (July 14, 2009) -- When an individual is injured by an allegedly defective product, he often sues all of the entities in the chain of distribution. When faced with such a product liability claim, immediately consider whether there are third parties, including "upstream" entities, which may be obligated to defend or indemnify your client.

If so, there may be an opportunity to immediately extract your client from the litigation or liability for the claim by tendering the defense of the claim to a third party. If that third party accepts the tender, your client is essentially off the hook for the claim with only minimal expense.

If the tender is denied, your client may still be forced to defend the claim, but may have further recourse against the party to whom the tender was directed.

Although not every case presents an opportunity to seek indemnity, product liability defendants, because of the general nature of their businesses, are often in a unique position to tender claims to third parties and obtain full indemnity.

The consideration should begin with the most likely source of a tender provision — a written contract. Indemnity provisions might be found in product supply agreements, licensing agreements, transportation contracts or global sales agreements.

Even purchase orders or invoices may contain indemnity agreements, often on the reverse side and commonly amidst a host of boilerplate provisions. In the absence of specific contractual language, some states provide for indemnity in product liability cases by common law or statute.

Regardless of the grounds on which the tender is based, a successful tender may be a company's best method of avoiding unwelcome litigation expenses.

Contractual Provisions

Companies most often transfer the risk of loss to others through insurance coverage. In addition to or in lieu of insurance, product sellers or suppliers often include, as a matter of course, contractual defense and indemnity provisions in their product supply agreements or purchase orders.

Such provisions are often easily overlooked since they are commonly included among the many terms written in smaller print or on the reverse side of a preprinted purchase order or supply contract.

A seller or supplier may use this type of document, including helpful indemnity language, with its customers, manufacturers or with contractors who assemble or install the products.

Generally, these provisions appear under the heading of "Indemnity", "Defense" or "Warranty" and include fairly standard language such as "Purchaser shall defend, indemnify and hold harmless supplier from and against all claims, including injury to persons or property, arising out of or in connection with the Purchaser's use of the product."

Despite their somewhat generic language, courts have upheld these types of provisions as a source of contractual indemnity. The interpretation and enforcement of these provisions, however, is often a matter of state law and counsel should carefully review the applicable law to evaluate any particular agreement.

Another potential source of contractual indemnity is an asset purchase agreement. Often claims relate to products manufactured or sold many years before the claim arose, and it is important to consider whether the product about which a claim is made is one for which your client even has responsibility.

A little investigation with a corporate historian or "old timer" may reveal that the product line was purchased, without assuming liabilities, from another company or that although the manufacturer of the product is now a subsidiary or affiliated company, the liabilities remained with a previous owner.

In those cases, the asset purchase agreement or merger documents will usually allocate liabilities and provide a specific procedure for notification of subsequent claims and lawsuits.

Common Law and Statutory Bases for Indemnity

In the absence of favorable contractual language, consider the common law of the jurisdiction. For example, in New York, "a party/distributor lower in the chain of distribution is entitled to common-law indemnification from the one highest in the chain of distribution."[1]

Similarly, in Texas, any member of a product's "marketing chain," including a manufacturer who incorporates defective products into its own product, "may receive indemnity from the manufacturer of the defective [part] or product."[2] Other states have similar provisions that may apply in the right circumstances.

A state statute may also provide the basis upon which to tender the defense of a claim. In Texas for example, Section 82.002 of the Texas Civil Practice and Remedies Code provides that "[a] manufacturer shall indemnify and hold harmless a seller against loss arising out of a products liability action.

Sellers under this statute, include distributors or retailers seeking indemnification against manufacturers as well as finished-product manufacturers seeking indemnification from component manufacturers."[3]

Practical Tips for Tender Letters

Once you determine that it is appropriate to tender a claim, it is important to make sure it is done correctly. The timing and content of a tender letter often have a direct correlation with the efficacy of the tender.

For example, a tender made too late, may be denied solely on the basis of timing. In most states, a statute of limitations governs when indemnity actions can be brought, and such statutes should be considered even at the point at which a claim is initially tendered.

It is also important to consider whether the agreement or the law of the jurisdiction provides a specific time period in which a tender can be made. Additionally, some contractual provisions, and the common law of some jurisdictions, require only that a tender of defense and indemnity be made within a "reasonable" time.

In a tender letter, a party should lay out the basis for the tender, including specific citation to contractual provisions, common law or statutes and include a copy of the relevant contract, if applicable.

The language in the letter should mirror that of the contractual provision relied upon and/or law on which the tender is based, but should always request full indemnity as to any

settlement, judgment or other expenses, as well as request the immediate defense of any claim or lawsuit.

It is important that the tender letter originate with, and be directed to, the appropriate individual. A tender letter can come from outside counsel or from an in-house attorney depending on the addressee and on the stage of the litigation.

The contract that provides the basis for the tender may list specific names and addresses of individuals who are to receive such communications. If the agreement is silent and a lawsuit is already underway, it is probably more appropriate that the letter be sent by outside counsel.

If, however, no lawsuit has been initiated or the party to whom the tender is directed is not yet a party to the case, the letter may be more effective and better received if it is sent by someone inside the company to her counterpart at the company from which indemnity is sought.

There may be business considerations, such as an ongoing relationship, which affect the substance and timing of the letter as well as the likelihood that tender will be accepted. It is important to discuss any such considerations with your client in deciding the most effective manner in which to approach the tender.

Even if the receiving party does not immediately accept the tender, the fact that the letter was sent still provides your client with tremendous leverage to use in defending the claim or in obtaining a settlement from the receiving party.

First, the company to whom the tender was directed runs the risk of being found liable for attorney's fees and costs from the time the tender is made.[4]

Second, there may continue to be a basis for a cross-claim or third-party complaint for breach of an indemnification agreement or for common law or statutory indemnity. While the second option requires continued litigation, in the case of a significant claim it may be well worth the added effort.

Conclusion

Your commercial clients need to be aware of opportunities to tender the defense of new claims within applicable time limits. This makes it necessary for outside counsel to have a good understanding of a client's business and an awareness of any potential contracts or

"deal documents" that may provide the basis for a tender of defense.

An effective tender letter, sent early in litigation or upon receipt of a claim, may result in significantly reduced liability exposure for your client, as well as substantially lower legal fees. Look for opportunities to tender claims, and carefully draft your tender letters, in order to effectively protect your clients' rights of indemnity.

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The opinions expressed are those of the authors and do not necessarily reflect the views of Portfolio Media, publisher of Law360.

[1] Lowe v. Dollar Tree Stores Inc., 40 A.D. 3d 264 (N.Y. App. Div. 2007).

[2] Crane Carrier Co. v. Bostrom Seating Inc., 2002 TX 5950 (Tex. Ct. App. 2002).

[3] Gen. Motors Corp. v. Hudiburg Chevrolet, 199 S.W.3d 249 (Tex. 2006)

[4] Under Alaska law, for example, an innocent supplier of an accused defective product may be entitled to indemnity from the product manufacturer for attorney's fees and costs in defending a claim even if no liability is ultimately found. Palmer G. Lewis Co. Inc. v. ARCO Chemical Co., 904 P.2d 1221 (Alaska 1995).
