



## What That “Boilerplate” Contract Language Can Mean to Your Business

By Jack Barone

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In the business world, many of us review contracts on a daily basis and certainly no one enjoys spending hours reading pages of boilerplate contract language. But how many of us bind ourselves to contract provisions saying “I’ve seen that before. It’s just standard”, without actually truly understanding what is being promised? Glossing over what one considers boilerplate language in a commercial contract can have devastating results on your business and should not be considered lightly.

One of the most commonly misunderstood, and perhaps most commonly litigated clauses in today’s contracts are indemnity provisions. Indemnity clauses are risk shifting devices used to allocate losses between the contracting parties. The language of such provisions can vary from requiring a contracting party (indemnitor), to compensate the other party (indemnitee) for a loss that was caused by the indemnitor’s negligence, all the way up to language obligating the indemnitor to “defend, indemnify and hold harmless” the indemnitee from any and all possible losses arising out of the contract regardless of the fault of others. Such provisions, known as “specific indemnity” in Arizona, are common today and could leave a party paying for losses beyond their reasonable expectations. Public policy will prevent one party from indemnifying the other for their sole fault or willful misconduct. However, a party may have to pay for the fault of another so long as it is not their sole fault. Indemnity provisions may also require an immediate obligation to defend the other party in a legal proceeding regardless of the duty to pay for the loss. These legal expenses can be astronomical. Understanding Arizona’s treatment of indemnity provisions is essential to ensure a party is not agreeing to take on more risk than intended.

Insurance clauses are also common in many commercial contracts. These clauses range greatly in scope from a simple requirement that a party have one or more types of insurance, such as commercial general liability, workers’ compensation, and motor vehicle, to much more stringent requirements mandating insurance limits of specified amounts, and that insurance be maintained for a specified period of time after completion of the contract. Furthermore, it is not uncommon for an insurance provision to require a party to name the other party as an “additional insured.” Provisions can even require that the policy be the primary over the other party’s own insurance. The full impact of such provisions may not be fully realized for several years, until a dispute arises. The consequences of violating contract insurance requirements can be catastrophic. In many cases, what is being required by the contract is not commercially available in the current insurance market. In the case of contractual insurance provisions, it is important know exactly what the policy provides and what one can expect in the event of a claim, before agreeing to provide a level of coverage that may not be available or reasonably affordable.

Another “boilerplate” contract provision addresses alternate dispute resolution, which frequently is identified as an “Arbitration” provision. These also can range widely from a requirement to mediate a dispute arising from the contract, to mandating your participation in a binding arbitration process, as opposed to litigating your dispute in court. Arbitration was often favored as a faster and less costly alternative to litigation in court. More recently, binding arbitration can often result in costs and time comparable to litigation, but without the ability to appeal to a higher level tribunal. Prior to agreeing to arbitrate, parties should consider whether the arbitration will be binding and understand the substantive right to a jury trial or appeal that may be lost.

Liquidated damage provisions are commonly found in commercial contracts. Liquidated damages frequently arise in contracts for performance, where a party’s breach results in an assessment of a predetermined financial “penalty.” They are commonly used in contracts where the damages for a breach may be difficult to determine. Such provisions can also spell out an amount that will be assessed, on a daily basis, for failure to meet certain contractually established deadlines for performance of the work. The primary consideration in reviewing such provisions should be, is the amount of damages specified reasonable and comparable to actual losses that are likely to be incurred in the event of a failure to perform. Less obvious, however, is consideration of what events trigger such damages, and whether there is any provision to allow an opportunity to remedy a failure and avoid the imposition liquidated damages.

While this is certainly not an exhaustive list of all possible boilerplate contract clauses, it is an attempt to provide important examples of provisions that can have a profound economic impact on your business, if not properly considered. Your level of “contract savvy” should determine your need for further review with your legal counsel and perhaps your insurance agent.