

## NDAAs Shine Spotlight On Contractor Indemnification

By Dietrich Knauth

*Law360, New York (January 10, 2013, 8:39 PM ET)* -- After an outcry over the U.S. military's indemnification of a contractor that exposed National Guard troops to toxic chemicals, the 2013 defense bill is trying to walk a fine line between putting such indemnification agreements under a microscope while preserving the military's ability to use such agreements when absolutely necessary, experts said.

Section 865 of the NDAA requires the secretary of defense to report to Congress after entering into a contract with an indemnification provision "relating to bodily injury caused by negligence or relating to wrongful death," including a written justification for the provision. The section's author, Ron Wyden, D-Ore., has said that the addition will increase contractor accountability and prevent taxpayers from footing the bill for negligent and willful actions.

The provision is a response to an indemnification clause in a KBR Inc. contract that could put taxpayers on the hook for an \$85 million jury verdict in favor of Oregon National Guard troops who were exposed to sodium dichromate, a known carcinogen, while guarding a KBR-operated water treatment facility in Iraq.

"We have seen that without accountability, companies like KBR are willing to needlessly put the lives of our soldiers at risk," Wyden said in December, when Congress included his amendment in the final version of the NDAA. "This contractor got a get-out-of-jail-free card at the taxpayer's expense with Congress and the public left completely in the dark."

While Section 865 does not prevent the use of contractor indemnification agreements, it will subject such agreements to more public and congressional scrutiny, making the Pentagon more reluctant to include such agreements during negotiations with contractors, according to experts.

"Senator Wyden's indemnification amendment is a great step in preventing the government from entering secret agreements to bail out contractors for their negligence," said Scott Amey, general counsel for the nonprofit Project on Government Oversight. "More should be done to restrict these agreements, which should be used on very limited bases."

The Professional Services Council, a contractor trade group, said it doesn't object to the provision as written.

"If the agencies can't justify an indemnification agreement, then there should be questions about why they are entering into it," Alan Chvotkin, general counsel for PSC, said. "My only hope that this reporting obligation does not in any way chill the department from entering into indemnification agreements when appropriate."

In order to convince contractors to do dangerous work, DOD sometimes has to protect them from liability costs that are otherwise uninsurable, Chvotkin said. But such provisions are rare, and are mostly limited to research and development contracts and environmental cleanup under the Comprehensive Environmental Response, Compensation, and Liability Act.

The indemnification seemed to be appropriate under KBR's Logistics Civil Augmentation Program contract, because of the open-ended risks that the government was asking KBR to undertake, Chvotkin said.

“Under that LOGCAP contract, KBR could have been directed to perform any number of actions that were unspecified at the time of the contract award, so as part of the negotiation, the Army decided to indemnify KBR,” Chvotkin said. “Other than R&D and CERCLA, I don't believe the DOD has written that many indemnification provisions. I'd be surprised that there were more than a handful written over the past few years.”

Stephen McBrady, a counsel in Crowell & Moring LLP's government contracts practice, said the indemnification agreements can be an important backstop to ensure that injuries caused by contractors — like the injuries suffered by the Oregon guardsmen — are compensated at the end of the day.

“It's important to remember that under the right circumstances, indemnification serves a valuable purpose,” McBrady said. “First and foremost, indemnification ensures that the people who are injured get paid.”

Before a 1998 law that streamlined government reporting, agencies were required to report annually to Congress on any contractor indemnification with a potential liability of \$50,000 or more, McBrady said. The NDAA will restore some transparency to the process, while allowing the Pentagon to use indemnification for cases of unusually hazardous risks.

“When you're talking about contractor indemnification, some level of transparency is important,” McBrady said. “This change reflects the reality that indemnification requests are going to be increased scrutiny by Congress and the public.”

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