

LITIGATION INFORMATION MEMO

DECEMBER 8, 2022

Attention Corporations, Partnerships and Other Contracting Parties! Is the Indemnification Clause in Your Agreement Broad Enough?

On Oct. 20, 2022, the New York State Court of Appeals issued a brief but consequential decision in *Sage Sys., Inc. v. Liss*, --N.E.3d--, 2022 N.Y. Slip Op. 05918 (Oct. 20, 2022), reversing a long-standing contract interpretation presumption relating the recoverability of attorneys' fees and costs resulting from disputes between contracting parties, or "intra-party" indemnification.

The issue in *Sage System* was whether the prevailing party in a partnership agreement dispute could recover attorneys' fees and costs incurred defending a dissolution action, where the partnership agreement included the following broad indemnification clause:

The partnership and the other Partners shall be indemnified and held harmless by each Partner from and against any and all claims, demands, liabilities, costs, damages, expenses and causes of action of any nature whatsoever arising out of or incidental to any act performed by a Partner which is not performed in good faith or is not reasonably believed by such Partner to be in the best interests of the Partnership and within the scope of authority conferred upon such Partner under this Agreement, or which arises out of the fraud, bad faith, willful misconduct or negligence of such Partner.

New York has traditionally followed the "American Rule" – that a prevailing party cannot recover attorneys' fees and litigation costs absent an express statutory or contractual basis for such recovery. Applying this rule prior to *Sage Systems*, courts often awarded the prevailing party costs and fees if the contract in question included a broad indemnification clause, even if disputes between the contracting parties were not expressly referenced in the clause. This is precisely what the Appellate Division, First Department did when it reviewed the partnership agreement in *Sage Systems*, concluding that the "broad language" of the indemnification clause "encompasses the recovery of attorneys' fees." 193 A.D.3d 624 (1st Dep't 2021). The Court of Appeals disagreed. In reversing that decision, the Court specifically noted that despite the broad indemnity clause in the partnership agreement, there was "nothing in the provision nor the agreement as a whole" that made it "unmistakably clear" that the partners intended to permit recovery for attorney's fees in an action between them on the contract." While this conclusion is not, technically speaking, a departure from the American Rule, it is a departure from the long-standing application of that rule by New York courts.

The practical implications of the *Sage Systems* decision are twofold. The first is directly addressed by the Court of Appeals in its decision: in preparing and drafting contracts, parties must clearly indicate their intent to include recovery of attorneys' fees and costs for a prevailing party of an intra-party dispute and should ensure that the language in the indemnification clause expressly states as much. Second, parties to contracts drafted prior to the *Sage Systems* decision that intended their broad indemnification clauses

to cover intra-party disputes should review the precise language of such provisions and consider amending them if their intent is not already “unmistakably clear” from the express language of the contract.

If you have any questions about the contents of this information memo, please contact Mara Afzali or any member of Bond’s [litigation practice](#).

