MEMORANDUM

State Of Alaska

Department of Law

To:	David W. Márquez Attorney General	Date:	August 23, 2005
Through:	Scott Nordstrand Deputy Attorney General	File No.:	#661-05-0132
		Tel. No.:	(907) 269-5274
From:	Craig J. Tillery, Environmental Section Chief Gail Voigtlander, Torts & Workers' Compensation Section Chief James E. Cantor, Transportation SectionChief	Subject:	Indemnification Agreements by State Officials

Question

You have asked whether a state official may legally agree, on behalf of the state, to indemnify another person or entity for a specified liability. As a general rule, a state official may not enter into indemnification agreements.

Analysis

The fundamental question to be resolved is whether there are restrictions on the authority of a state official to enter into an agreement containing a provision that requires the state to indemnify another party to the agreement. Such restrictions may arise under the state constitution, statutes, or regulations. In this instance, a provision of the Alaska Constitution, implemented by a statute, provides the basis for our conclusion that the authority of state officials to enter into indemnification agreements is very limited.

The restriction on indemnification arises from the operation of article IX, section 13, of the Alaska Constitution ("Section 13"). That section provides, "[n]o money shall be withdrawn from the treasury except in accordance with appropriations made by law. No obligation for the payment of money shall be incurred except as authorized by law." The first clause of Section 13 generally demands that expenditures can only be made from legislative appropriations, while the second clause proscribes state employees from incurring future liabilities (such as liabilities arising from indemnity provisions) without statutory authorization. During debate at the Alaska Constitutional Convention, Section 13 was described as "a standard section providing that money shall not be withdrawn

from the treasury except in accordance with appropriations made by law." 2A *Proceedings of Alaska Constitutional Convention* 1111 (December 19, 1955). A delegate to the Alaska Constitutional Convention fleshed this out during debate over Article IX, stating, "[y]ou contract administratively after the legislature has authorized such a contract." 5A *Proceedings of Alaska Constitutional Convention* 3406 (January 28, 1956). This statement supports the view that the constitutional provision requires that legislative authorization precede any action by the executive to obligate monies from the state treasury.

Article IX, section 13 is implemented by AS 37.05.170. *See Zerbetz v. Alaska Energy Ctr.*, 708 P.2d 1270, 1277 (Alaska 1985). That statute provides in relevant part that "obligations may not be incurred against a fund unless . . . an appropriation or expenditure authorization has been made for the purpose for which it is intended to incur the obligation."

No Alaska case law directly construes the application of either Section 13 or AS 37.05.170.[1] However, these provisions have been addressed twice in Attorney General opinions. In each instance, we said that these provisions of law prohibit state officials from providing indemnification. We first addressed this question in 1992 *Inf. Op. Att'y Gen.* (Jan. 1; 663-92-0041). There the state was responding to a demand by the Matanuska-Susitna Borough that the state agree to indemnify the borough for the borough's exercise of erosion control powers. We noted that, "in essence, an agreement to indemnify constitutes an agreement to obligate state money to cover the potential liability." 1992 *Inf. Op. Att'y Gen.* at 3 (Jan 1; 663-92-0041). Citing to AS 37.05.170, we determined that state officials are prohibited from providing indemnification in the absence of an appropriation against which the obligation may be charged. *Id.*

The issue was raised again two years later with respect to the potential liability of the Alaska State Emergency Response Commission. In the 1994 informal opinion we discussed with approval the earlier opinion. 1994 *Inf. Op. Att'y Gen.* at 2 (Jan. 25; 663-

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[1] Application of Section 13 and AS 37.05.170 was briefly addressed in *Zerbetz*. In that case, the plaintiff sought enforcement of the terms of an employment contract. The state claimed the contract was void because it violated the terms of Section 13 and AS 37.05.170 by creating an unfunded obligation. The court, at the plaintiff's urging, drew "a distinction between the question of the contract's validity and the ways in which [a party] might enforce it." *Zerbetz*, 708 P.2d at 1277. The court then held that "even though no appropriation exists to cover the contract's obligations," and the state could refuse to pay under Section 13 and AS 37.05.170, Zerbetz had "a specific, albeit uncertain, remedy: the chance to have his claim presented to the Legislature." *Id.* at 1278.

94-0390). Relying on the restrictions contained in article IX, section 13 and AS 37.05.170, we stated that "unless there is an existing appropriation to cover the state's potential liability, state officials are prohibited from providing indemnification." *Id*. at 2.

In response to similar legal authority, the United States and other states have reached similar conclusions. *See, e.g.,* 78 *Wis. Op. Att'y Gen.* 1 (Jan. 18, 1989); *Chase v. United States*, 155 U.S. 489 (1894); *Hooe v. United States*, 218 U.S. 322 (1910); *Sutton v. United States*, 256 U.S. 575 (1921); *Leiter v. United States*, 271 U.S. 204 (1926); *Goodyear Tire and Rubber Co. v. United States*, 276 U.S. 287 (1928); *Shipman v. United States*, 18 Ct. Cl. 138 (1883); *City of Los Angeles v. United States*, 107 Ct. Cl. 315, 68 F. Supp. 974 (1946); 35 *Comp. Gen*. 85 (1955).

Thus, we reaffirm our longstanding view that a state official may not enter into an unqualified indemnification agreement in the absence of an existing appropriation to cover the potential payment that may be required of the state. To find otherwise could create a financial obligation of the state without prior legislative authorization in contravention of article IX, section 13 and AS 37.05.170.

However, we also recognize that in some instances unique commercial realities might compel some accommodation for requests for indemnification. There are several possibilities. First, as we noted in the 1994 opinion, it is possible for the legislature to designate a fund and appropriate sufficient monies into that fund to satisfy the requirement for prior appropriation and thereby allow for indemnification agreements. *See* 1994 *Inf. Op. Att'y Gen.* at 2 (Jan. 25; 663-94-0390). For the reasons stated in the 1994 opinion, appropriation into a fund may not work in situations involving large or complex potential liabilities, but it may work quite well for simpler cases.

Second, an indemnification can be qualified, if the qualification is adequately worded. However, a qualified indemnification should be used in the rarest of circumstances and only when approved at the highest levels because even qualified indemnification clauses are inadvisable. This is true for several reasons. First, qualified indemnity clauses may inadvertently mislead a party into believing that they have secured a legally enforceable indemnification provision.[2] Second, in some instances it may not be possible for the legislature to appropriate monies to cover an indemnification without running afoul of the public purpose doctrine found in article IX, section 6 of the Alaska

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[2] Even if a party believed this, or in fact secured an unqualified indemnification, the provision would likely remain unenforceable as against the state because the agreement to include it would be an act outside the authority of the state official. *See California-Pacific Utils. Co. v. United States*, 194 Ct. Cl. 703 (1971).

Constitution. *See*, *e.g.*, 2003 *Inf. Op. Att'y Gen.* at 3 (Nov. 18; 883-03-0044) (The payment of a debt to which the state is not a party confers no benefit on the public, and "failure to confer a public benefit violates the public purpose doctrine set out in art. IX, sec. 9 of the Alaska Constitution."); 2002 *Inf. Op. Att'y Gen.* at 6 (June 28; 883-02-0058) ("Use of state money to pay a litigation-based settlement, in which the state was not a party, raises significant legal questions as to whether the expenditure would be for a public purpose.").

Third, a qualified indemnification agreement may morally obligate the legislature to pay for the financial obligation. 1994 *Inf. Op. Att'y Gen.* at 2 (Jan. 25; 663-94-0390). As such, a qualified indemnification agreement could have the effect of pressuring the legislature to appropriate money when it would not do so if its decision was unfettered.[3]

Thus, a qualified indemnification agreement should only be given in those rare cases where it is absolutely necessary and would be a benefit to the public. The decision of whether to agree to a qualified indemnification should be made at a high level of state government (such as by a deputy commissioner) and then, only with the concurrence of the attorney general or the deputy attorney general. Lastly, if qualified indemnification is given, it should clearly state that the legislature has unfettered discretion as to whether to appropriate the money. In the past, some state officials have signed agreements in which the state agrees to indemnify a party "to the extent permitted by law" or "subject to appropriation." These simple qualifications should be expanded to ensure that other parties to the agreement are fully informed about the limitations in the statement of indemnification, including the need for a specific appropriation for that purpose.[4] An example of language that would be sufficient is as follows:

> Subject to a specific appropriation by the legislature for this purpose, the [agency] agrees to indemnify [the party] for [the liability]. All parties to this agreement recognize and agree that the agency has no appropriation currently available to it to indemnify [the party] under this provision and

[3] Such moral obligations have been called coercive deficiencies and held to violate the federal Anti-deficiency Act by the United States. 1986 *Inf. Op. Att'y Gen*. at 1 (June 3; 665-86-0057).

[4] This language would address arguments analogous to that raised in *Cherokee Nation of Oklahoma v. Leavitt*, ___ U.S. ___, 125 S. Ct. 1172 (2005) that even though a government contracting officer lacked authority to bind the government without regard to the availability of appropriations, the government was nonetheless bound by its promises to pay contract support costs where it had appropriated adequate unrestricted funds.

> that enactment of an appropriation in the future to fund a payment under this provision remains in the sole discretion of the legislature and the legislature's failure to make such an appropriation creates no further liability or obligation of the [agency].

Conclusion

For the reasons stated, a state official is without authority to sign an unqualified indemnity agreement unless there is an existing appropriation sufficient to cover the full amount of any potential liability. Although the state may agree to indemnify if the indemnification is qualified in accordance with this opinion, a qualified indemnification agreement should (1) clearly explain that the decision of whether to appropriate funds necessary to pay the liability is within the unfettered discretion of the legislature, and (2) be entered only with the approval of high level state officials and the concurrence of the attorney general or deputy attorney general.