
Contractual Indemnity

Most commercial agreements (e.g., leases, vendor agreements, and construction contracts) contain indemnification or “hold harmless” clauses. In these clauses, one party (i.e., “the indemnitor”) agrees to bear responsibility for the specified losses, damages, or liabilities of another party (i.e., “the indemnitee”). This handout provides an overview of contractual indemnity clauses and issues affecting their enforceability.

Types of Agreements

There are two basic types of indemnity agreements. Those that indemnify against loss or damage and those that indemnify against liability. Where the agreement is one for loss or damage, no recovery can be obtained until the indemnitee has suffered actual damage or loss. Liability indemnifications do not require actual damage or loss, and indemnification may be had as soon as the liability becomes fixed and established.

Scope of Indemnification

The scope of obligation that an indemnitor assumes will vary depending on the specific wording of the agreement. In general, the indemnification obligations fall into one of three categories. They are:

- *Broad indemnification* - the indemnitor agrees to be responsible for all liability arising out of the agreement, regardless of who was responsible for the loss.
- *Intermediate indemnification* - the indemnitor agrees to be responsible for all liability arising out of the agreement, except where the loss is caused by the sole negligence of the indemnitee.
- *Limited indemnification* - the indemnitor agrees to be responsible only for losses caused by its sole negligence.

For complex transactions, an agreement may specify different obligations for different covered acts. Such indemnification is sometimes called hybrid indemnification.

Covered Losses or Liabilities

The agreement should specify the types of losses or liability it covers. As a general rule, courts will not enforce an indemnity agreement against a party for losses or liabilities that are either undisclosed or not reasonable within the terms of the agreement or the intent of the parties. Typical items specified include: direct losses and damage, consequential losses and damage, and defense costs and other litigation expenses.

Enforceability

As a general rule, a promise to indemnify will be valid and legally enforceable as long as: the covered act is not illegal, immoral, or against public policy; the agreement conforms to the general rules governing all contracts within the jurisdiction; and the agreement does not conflict with any statutory requirements. Contract rules require there be fair notice of the indemnity provision and that the agreement be clear and unequivocal, be bargained for, and be supported by valid consideration. The majority of states have laws called anti-indemnification laws that limit a party’s ability to transfer liability for injuries caused by sole negligence. It is important that all indemnification agreements be drafted or reviewed by knowledgeable legal personnel.

Financial Responsibility

An indemnification agreement should be practically enforceable, as well as legally enforceable. To ensure that an indemnitor has the financial ability to meet their obligation, most commercial agreements also require that the indemnitor maintain sufficient insurance coverage or provide other financial assurances. It is important to read these financial responsibility requirements in tandem with the indemnity requirements to determine the expected degree of obligation or protection afforded by the agreement.