

Indemnification provisions

Before you sign a contract, take time to understand indemnification clauses

Business executives often spend a considerable amount of time negotiating the contract terms they deem the most critical while others are merely glanced over.

As such, monetary terms, warranties, lead times, contract length, termination and noncompete covenants typically generate a lot more passion than indemnification or “hold harmless” clauses.

Smart Business spoke with Isabelle Bibet-Kalinyak, an Immigration and Health Care Corporate Attorney at Brouse McDowell, in order to better understand the purpose and importance of these technical provisions.

What are indemnification clauses?

Risks are inherent to all types of contracts. Indemnification is the process whereby one party seeks to secure another party against anticipated losses or damages. It is a contractual tool that allocates in advance the risks or losses associated with the contractual relationship, whether such risks or losses are suffered by the parties to the contract or a third party.

Why are indemnification clauses important?

Indemnification or ‘hold harmless’ clauses have become universal in the business world. Although initially most common in the construction industry, they are now pervasive across all industries and contract types by default.

Parties should carefully review all indemnification terms because they

may cause substantial financial losses (including, at times, reimbursement for all legal fees) to the indemnifying party if successfully invoked.

Are indemnification terms required in all contracts?

The parties should analyze the necessity and scope of the indemnification terms to best fit their respective needs and risk tolerance. Express indemnification terms may not be required when insurance (general liability, medical malpractice, etc.) for the risks or losses at stake is already part of the deal.

Further, various common law principles already allocate vicarious or derivative risks based upon the relationship between the parties.

For example, under the legal doctrine of respondeat superior, an employer is responsible for the wrongful acts of its employees, and under the doctrine of agency by estoppel, a principal is liable for the acts or omissions of its apparent agents. These common law doctrines vary from state to state.

Are indemnification clauses legal?

Indemnification clauses are legal, for the most part. Their proliferation and abuse have, however, triggered



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statutory limits at the state level, notably in the construction industry and landlord-tenant context. Some states now prohibit certain transfers of risk or void clauses that attempt to pin all liability on one party, even when concurrent negligence exists.

What are some key elements executives should discuss with legal counsel?

Executives should not forego all negotiations relative to indemnification merely because of relatively unequal bargaining power between the parties.

The parties should at least review and weigh the following elements of the clause, particularly when the stakes are high: necessity, scope, types of risk transferred (acts, omissions, concurrent negligence, etc.), defense, defense/legal costs, duration and termination, effect of settlement, damages limitation, insurance coverage, effect of merger and acquisition, statutory limitations at the state and federal level, and regulations (Medicare).

Amending the language or establishing reciprocity can help mitigate the risks. Indemnification clauses are risky and complicated. Understanding exposure and specific terms is key prior to signing on the dotted line. ●