

Advanced Contracts, Tendering and Public Procurement
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Special Contracts: Indemnity Part 01

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Indemnity contracts



- **Section 124**

- Promise by one party to save the other against the loss. There is a promise to compensate the other person.
- When A conveys to B that if the goods are supplied to C, he will see that B gets paid, there is a contract of indemnity and in such a situation, A is the indemnifier and B is the indemnity holder.
- Essentials of Indemnity
 - *Anticipated loss.*
 - *Must have all the requirements of a valid contract.*
 - *Intention to save the other party*
 - *Express or implied contract*
 - *Presence of good faith.*
- Insurance contracts as indemnity?
- Implied Indemnity
 - Section 169 and 145 of the Indian Contract Act, 1872 talk about implied indemnity.
 - Even under sec. 222 of the aforementioned act, the employer of the agent is bound to indemnify him against the consequence of all the lawful acts done by such agent in exercise of the authority conferred upon him.
 - Under Partnership Act, 1932, sec. 10 and 13 deal with implied indemnity.



The Indian Contract Act 1872 and which in current times in contemporary contracts assumes a great amount of significance in terms of say having a clause in a contract or trying to cover their losses through such contracts and that is called indemnity contracts. Now, indemnity contract is a special category of contracts and it is covered with indemnity and guarantee as it is called. it has only two sections that are dedicated to trying to define and understand indemnity and the courts have rightly said that these two sections do not entirely state what the law of indemnity is and you can infer the laws of indemnity in several other provisions of the Indian Contract Act itself and with reading of other sections of the law.

Like in the Companies Act, can directors claim indemnity from the company. So, if you look at the Partnership Act, can partner claim indemnity from the firm? So, there are numerous instances of these indemnity that exists and hence to understand what indemnity is you will notice that there are two parties to this contract. One is called the indemnity holder who has , the promise to be indemnified and one is called the indemnifier who has the responsibility to indemnify.

In a contractual relationship, there are two parties involved: the indemnified party and the indemnifier. Interestingly, the concept of indemnity, which means to provide compensation or cover for losses, is referred to as the "hold harmless" clause in UK law. To indemnify

means to assure the other person that their losses will be covered. It signifies the commitment to fulfill the contractual obligations and compensate for any losses incurred by the indemnified party. This ensures that the other party can proceed with the contract without worrying about potential damages or losses, as the indemnifier takes responsibility for them.

The promise of indemnity which means that you do not want your contracting partner or your contracting party to suffer any kind of a loss that arises from the contract itself or may arise from your actions as the case maybe, and hence in modern commercial contracts not modern even quite from early times the most essential negotiated clauses in most modern-day contracts is the clause of indemnity.

Section 27 and Section 23 today an employment bond is also titled as an indemnity bond. So, you expect the employee to indemnify the employer in case he forfeits the term of the contract or lease the term of the contract before the time stipulated for any kind of loss that may arise from his leaving of the employment that is what indemnity means.

The essentials of indemnity is that when one gets into such a contract or such a clause in a contract you anticipate that there can be loss that one of the parties the contract may suffer or both the parties may suffer. In modern context you will notice that indemnity if you look at the law and the broader context of the same it is usually mutual it cannot be just one party promising the other.

The mutuality principle plays a significant role in indemnity agreements. Both parties involved must have an implied obligation to compensate the other if they cause any losses. It is a mutual understanding that if one party commits a loss, they will be responsible for providing compensation. This division of responsibility can be explicitly expressed in the contract. There is an anticipation that one party may experience some form of loss, and the contractual agreement ensures that the necessary provisions are in place to address such situations.

And intention when agreed to the indemnity clause is that want to save the other parties from any such purposes and in good faith when you do the same whether there is an express or an implied contract does not matter, you have a duty to indemnify. So, that is how the contract of indemnity plays an important and a critical role in today's context.

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- **Indemnity promise to save others from the loss**
 - Human factors?
 - Natural factors?
 - Accidents?
- An indemnity contract arises when one individual takes on the obligation to pay for any loss or damage that has been or might be incurred by another individual. The right to indemnity and the duty to indemnify ordinarily stem from a contractual agreement, which generally protects against liability, loss, or damage.
- **Types of Indemnity**
 - Professional indemnity: Offers protection to an individual and his business against the claims for professed negligence or breach of duty arising from an act, error or omission in the performance of professional services. (Contractual indemnity)
 - IP Indemnification: Software breach of warranty or copyright infringement, especially platform-based.
 - Product Indemnity.
- **Damages v. Indemnity**
- **Insurance v. Indemnity**
- **Limitation of Liability v. Indemnity**



What does indemnity do? It promises the other to save from the loss that is caused by his own actions that is when you strictly read Section 124. So, from the act of the promise or any other intention that is where Section 124 is only about such kind of losses that maybe caused just by the contracting parties' behavior, conduct or his contractual relationship.

However, indemnity is far broader than that because you notice that you may loss because of not only my fault, you may suffer loss in this contract because of natural factors and natural factors could be a cyclone an earthquake, a volcano, a tsunami, or flood so on and so forth. So, there again you talk about saying look once you enter a contract and in case you suffer losses from these natural factors then I will compensate you do not worry please go ahead and fulfill your obligations in this contract.

So, that could be also a kind of a loss that needs coverage that needs some kind of anticipation to be factored into as well. Also, you will find that losses can be caused due to accidents. So, when someone is producing some machinery for you or you are handling someone else's machinery there machinery can meet with an accident and then you expect the manufacturer to say look in case while operating this machinery if you suffer any kind of loss or if there is an accident that occurs due to the handling of this machinery, I will compensate and indemnify have the confidence by this machinery. So, the indemnity clause is usually used as a guarantee to the performance of a product. It is also used to give confidence to the parties saying that any kind of loss will be covered due to my inactions and

accidents usually are not necessarily that can be caused by humans or natural facets it can be simply a patent or a latent defect in the machinery.

It is not necessarily a human error or human factor that has to be taken into consideration and those accidents are also something that indemnity may want to cover in the long distance and has some important significant implication. How do you look at the different kinds of indemnity in India and abroad.

Different kinds of indemnity are discussed further. For example, intellectual property indemnification is the most popular one, IP indemnification as it is called. This is a case where a patent holder, inventor, or a manufacturer says that if you buy this product, I am giving you the license to this product because I have IP to it.

Tomorrow if someone else files an infringement suit against you and then you must defend it and you suffer any kind of a loss because of that infringement. So, I will promise to indemnify you for that kind of a loss or that kind of a hardship that you undergo because you have taken an IP license. So, that is a promise that holders of intellectual property get into.

And that is how an IP indemnification clause makes that kind of a promise. Product indemnity is based on the same example that I told you that I want you to take my product in the confidence that if while handling the products anything happens to you or your employees or any other person I will cover that loss, I will cover the risk, and I will indemnify them. Therefore, that is what a product indemnity would also mean.

Similarly, professional indemnity now this is interesting because you want professional indemnity to be there when suppose I am sending one of my employees to do some onsite work and due to his actions or inactions you suffer any kind of a loss or injury due to his professional misconduct or otherwise. Then in those cases I must give you that assurance saying that look do not worry, allow our employees to come on site.

If anything, they do due to which you suffer any loss I will compensate you for the same that is an assurance that is the promise that is usually given in professional indemnity. So, you will again see the dimensions of indemnity and the applications of the same that are required as risk assessment in modern kinds of contract that must be generally undertaken and these have to negotiated and agreed upon.

Though there are different forms that are available on these kinds of indemnity clauses. This is basically how people design contracts in the modern context and this plays an important role in government contract, indemnity has an important obligation to be completed because you do not want contractors just to be giving you basic nominal damage or compensation which is how the law on damages works.

Indemnity is far broader in its application and scope than what damages is. Most of the government contracts have damages clause where they forget to have an indemnity clause. Now, damages clause of the limitations of damages is because under Section 73 and 74 of the Indian Contract Act you are entitled to only those kinds of damages that are reasonable in nature.

So, do not have any kind of damages that says you can get exemplary damage you have only nominal damages. Point two is there is something called rule of remoteness of damages which means you cannot get damage that is remote. The damages that can be foreseen, damages that are direct, are the only things that you can get as monetary quantification of the loss that you suffer.

Damages has certain limitation, damage has certain restriction, it has a huge jurisprudence of what you can claim and what you cannot claim. However, idea of indemnity is to broaden the liability of the other party to cover things that you may not have foreseen, things that may be due to the actions of the third parties, things about something that is indirect, something that is consequential.

Indemnity's basic purpose is to expand the whole law of damages which has huge limitation to what can be claimed and what can be asked. Indemnity is used to broaden the same and hence it becomes a very important and inevitable part of contractual discussion. Very often than not insurance contracts have been called as indemnity contracts.

They are in one sense. They are not once that are covered under 124, they are covered under the broad ambit of indemnity because the basic duty of insurance company is to cover your loss. So, you pay premium, you hope nothing will happen, but if something happens the insurance companies come and hold you harmless which means that not in the sense of a criminal conduct.

That is nothing like indemnity, but in the civil liability the insurance company they will say that we will compensate with the money and that loss is covered by money. So do not have any hesitation please go ahead with your business. So, fire insurance could be indemnity insurance and so on and so forth. So, most companies take some of these insurances which are critical and important.

Also, notice that today doctors take what will be called as professional indemnity insurance, why is this important is because doctors can be sued for medical negligence from the patients and very often than not if the doctors must pay compensation for medical negligence, then the professional indemnity insurance can be invoked and the insurance company will pay the patient that kind of a compensation.

The doctors need not pay from his own pocket so that is the kind of job or the responsibility that these professional indemnity insurance do. So, that is something that lot of professionals take including directors of the company because today directors are unfortunately going to be held personally accountable or liable, they inevitably want to cover that risk or transfer the risk with an insurance company.

And even directors of companies do take what we call as the professional indemnity insurance. So, if the director is personally sued by a shareholder or by any kind of an individual to which the director must contribute or pay, then the director will end up paying a lot of money and hence an insurance works in his favor.

The insurance company will step in like it does in case of doctors and it will pay that kind of an indemnity to those third parties as well. Interestingly, in indemnity there is no limitation of liability unless you want to cap it and you say for example in insurance, we take fire insurance, but my final responsibility is just 10 lakhs or 10 crores. So, that is the final limit that insurance company gives to users.

It is not unlimited in every sense of the term whatever is your loss we will cover it; no, it is a cap that usually comes into place. For example, we talk about indemnity bond in employment it is not unlimited so it could be 3 lakhs or 5 lakhs so that is what your indemnity liability is. So, you could have that kind of limitation of liability that is possible in terms of the amount and figures to which you should be held accountable to.

At the same time please note indemnity can be quite a broad in terms of third-party losses and liabilities. In terms of those that are foreseen, in terms of those that are consequential losses or damages and consequential is something that you know in most common law jurisdiction is not admitted whereas indemnity can help you gain those kinds of necessity losses as well.

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- **Implied Indemnity: Adamson V. Jarvis, 4 BING.66:29 R.R 503**
- **Facts of the case:** The cattle was given for sale to the auctioneer by a person named Jarvis who was not the real owner and, as per his instruction the auctioneer (Adamson) sold the cattle. Aggrieved by the wrongful conversion, the true owner held the auctioneer liable to pay the damages. Later, the auctioneer sued Jarvis to be indemnified for the loss that he suffered by way of damages to be paid to the real owner.
- **Issues Raised:** Whether all the damages that indemnity holders have been compelled to pay in any suit in respect of any matter to which the promise of indemnifier applies? Whether Adamson was entitled to pay damages as he was completely unaware of the fact that Jarvis is not the real owner?
- **Held:** The Court held Jarvis liable to pay the damages to the auctioneer as he misrepresented himself and failed to state the true facts about his ownership. As per section 125, rule 2, of ICA Jarvis was responsible for the loss of the auctioneer and the given situation compelled him to compensate the auctioneer.
- In another case, *Dugdale v. Lovering 1875*, the plaintiff was in the possession of certain trucks which were claimed by the defendants and one K.P. Co. The defendants demanded the delivery for which the plaintiff asked for an indemnity bond but received no response and went ahead and delivered the truck. Later, K.P Co. successfully sued the plaintiff for the conversion.
- It was held by the court that there was an implied indemnity from the defendants to make good the loss suffered by the plaintiff.



In matters of implied indemnity, it is important to understand that in common law and I think if you look at how the court in India have always viewed this provision. They say that look every contract is a contract of good faith it may not be of utmost good faith because insurance contracts are contract of utmost good faith, but every normal contract is a contract of good faith which means that due to the contracting parties own for they should not create a loss to the other parties.

This is something that is implied by the laws of obligation. If there is any such laws then have a duty to indemnify the other person. Normally we will say from that loss you will have to pay damages, but indemnity is also about the fact that look you are going to be held accountable, you are going to held liable and this is implied in law, implied in contract. So, you cannot from your promised obligation or from your contractual obligation, cause any loss or damage to the other party in the contract.

Implied indemnity has been in existence for quite some time and we know that in most cases where contracts come into existence the party that causes harm, promises to hold the other party harmless and any kind of harm must be compensated and equated in terms of the monetary loss or value and everyone has a right to claim the same irrespective of whether the

law defines it or irrespective of the fact that the contract has such a clause. That is the general nature of indemnity in the form of damages that ought to be always paid or covered and that loss is something that needs to be compensated as well.