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# How to Draft Better Indemnity Clauses





# Intro

## Introduction

*Indemnities are not a one-size-fits-all approach.*

Indemnification clauses need to be drafted while keeping in mind party-specific requirements and the context of the agreement. Attorneys borrow indemnity clauses from templates thinking they are “standard” or “boilerplate”, then suffer consequences. It results in covering risks that aren’t applicable to the deal or sometimes there’s inadequate risk coverage. Indemnity clauses are primarily about shifting risk from one contract party to the other. Using templates can lead to the risk transferring to the wrong person. It becomes a challenge to execute. Both parties suffer and end up arguing in courts.

Individuals and businesses that lack contextual drafting frequently fail to conduct a risk-appetite analysis. Requesting changes to the terms can seem horrifying to a client. Often they assume the terms cannot be modified. As a lawyer, you know this clause can be negotiated. But does your client know?

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When drafting, focus on ease and practical usefulness rather than imitating a template. Tailor the language for the commercial relationship and conduct a risk analysis. In this guide, we’ll discover a clear path that leads to indemnity clauses that are functional, feasible, and factual.

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# What is an Indemnity Clause?

An indemnity clause is a common yet tricky contractual provision that allows parties to manage contract risks. It's a risk allocation tool that transfers certain risks associated with one party to another. This clause is used when one party faces a higher risk of commercial loss, there is a possibility of third-party infringement, software is licensed, insufficient normal damages, or confidential information is at stake.

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*The reasons for indemnity are determined by the context of the agreement and the obligations of the parties.*



## WHAT IS AN INDEMNITY CLAUSE?



Laying the groundwork for an indemnity clause requires reducing uncertainty by operating under these four components.



The Vendor agrees to **indemnify, defend and hold harmless** the **Client, its officers, employees, agents, affiliates, representatives, consultants, and contractors** from and against any and all **losses, costs, penalties, fines, damages, claims, expenses (including attorney's fees) or liabilities** arising out of, resulting from, or in connection with **the services contained in this Agreement, physical harm, mental harm, harm to reputation, business loss, breach of confidential information, non-compliance with applicable law, illegal activities, infringement of third party rights, and/ or IP infringement.**"

1

These three terms have a distinct meaning. Using "indemnify" ensures effective risk management by making good the other party's loss. "Defend" is used when the indemnifying party bears all legal costs. "Hold harmless" shifts risk to yourself by accepting responsibility for the loss suffered by the other party.

2

The indemnifying party will not only compensate the client for the loss suffered but also the individuals associated with that party.

3

These qualifiers protect the client from potential third-party actions and provide comprehensive coverage for indemnification.

4

This emphasizes when the indemnity clauses will apply. Pay close attention to the arrangement between parties. For example, in a Supplier agreement, if the Supplier delivers defective or destroyed goods, this can result in business loss, and this condition should be specifically included. In this case, having an IP infringement condition may not be entirely appropriate or necessary unless a valid reason is explicitly stated in the agreement.



# Questions to Ask Before Drafting an Indemnity Clause

*Hasty drafting can lead to inadequate indemnity clauses that neither serve the clients or the deal.*

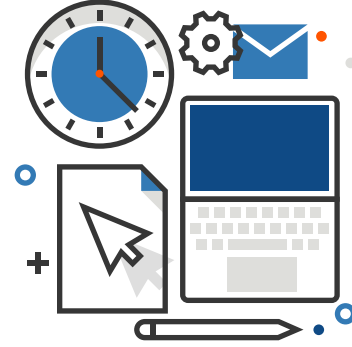


## QUESTIONS TO ASK BEFORE DRAFTING AN INDEMNITY CLAUSE



Questions are a great way to reflect on the facts and help us draft substantive clauses. Reflect, then draft.

First, contemplate whether you need an indemnity clause. For instance, you may not need one if the indemnity provides less protection for a breach of contract than the standard legal protection under the law.



- ✔ What types of losses must be covered by this agreement given the commercial relationship?
- ✔ Which party should be held responsible for each type of loss?
- ✔ How much will the indemnifying party pay in compensation for losses?
- ✔ What specific events or actions will trigger indemnification under this agreement?
- ✔ How long should this indemnity clause survive?

### TIP

A SMALL BUSINESS COULD FEAR NEGOTIATION WITH A BIGGER COMPANY THAT QUESTIONS THEIR COMPETENCE FOR REQUESTING INSURANCE COVERAGE. APPROACH THIS WITH CAUTION. WHEN CONTRACTING, CONDUCT A RISK ASSESSMENT AND CONSIDER YOUR LIMITATIONS.



# Drafting Considerations

The fundamental elements of indemnity will help you write a clause that is useful to your client. Next you need to consider the practical side, building on those fundamentals.





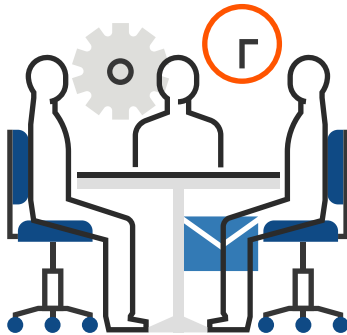
## DRAFTING CONSIDERATIONS

### Language Determines the Scope

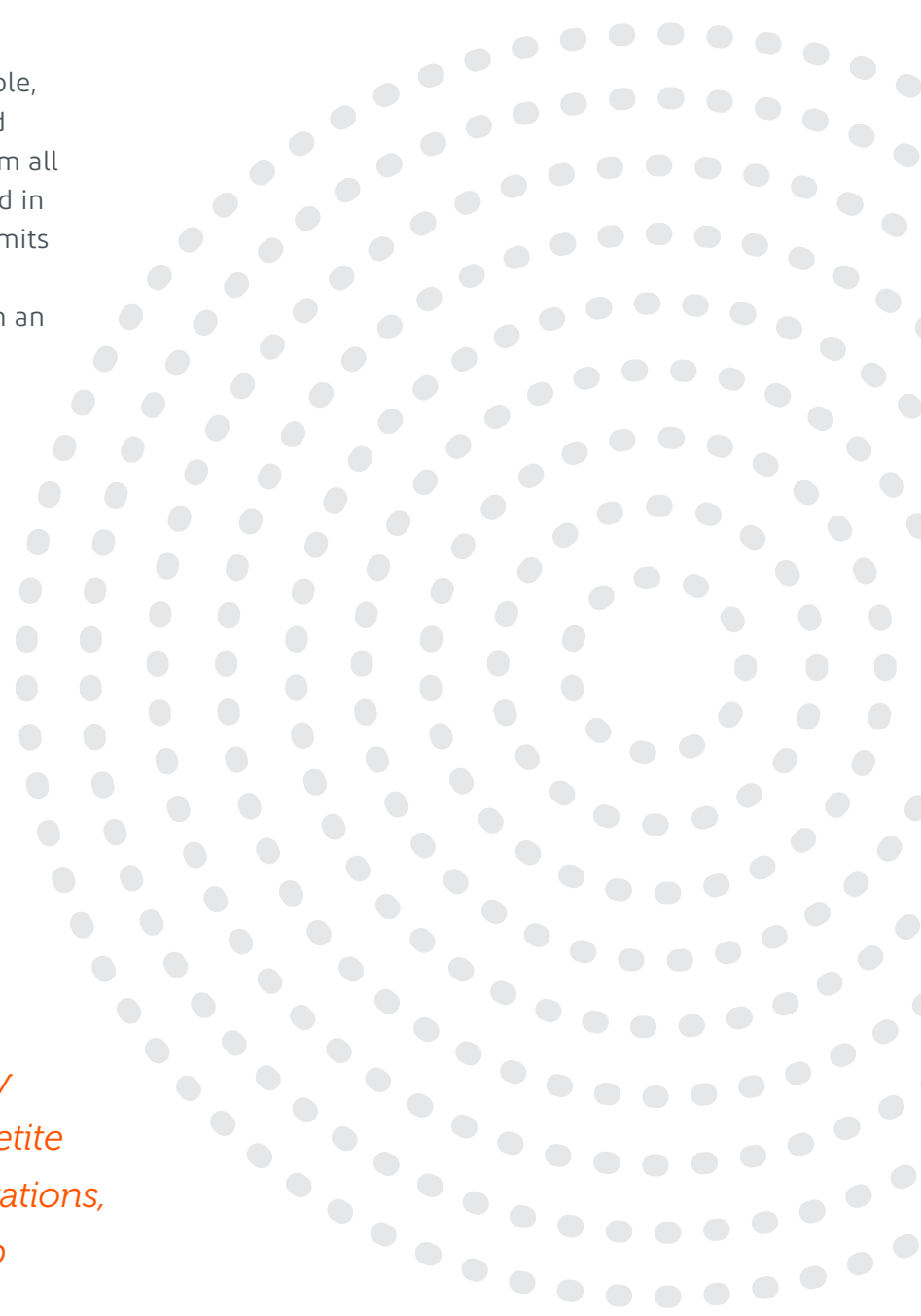


*No clause is wrong or right; it's all about context.*

Have transaction-specific language that conveys the intended meaning. For example, “The Vendor agrees to indemnify and hold harmless the Client and its employees from all liability arising from the services described in this Agreement.” This drafting language limits the scope of indemnification and specifies when indemnity will kick in. This results in an amicable clause.



*Draft a highly relevant indemnity clause by conducting a risk appetite analysis, considering party obligations, and the commercial relationship*





## DRAFTING CONSIDERATIONS (CONTINUED)

### Language Determines the Scope



Different ways the scope of indemnity clauses can be altered:



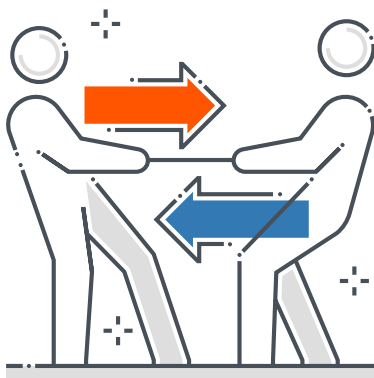
#### ✓ Reduce the number of qualifiers

A holistic clause covers all possibilities and leaves no risk of liability for the other party. The indemnity can be limited to specific events, a number of indemnitees, or an intended scope. Broad indemnity clauses are not a sure bet. When drafted, they frequently lead to ambiguous interpretations, which is a risk in and of itself.



#### ✓ Create mutual indemnities when possible

Be aware of one-way provisions in contract templates. Certain contracts necessitate one-sided indemnities. For example, when the onus of performance is on a Service Provider. Having a one-sided or mutual indemnity clause depends on the duties of a party in an agreement.



#### TIP

INSTEAD OF HAVING STRICT MUTUAL OR STRICT ONE-SIDED INDEMNITIES, USE LANGUAGE THAT COMBINES THE TWO. FOR EXAMPLE, YOU COULD REQUIRE ONE PARTY TO PAY FOR CERTAIN LOSSES AND DAMAGES WHILE ALSO TRANSFERRING SOME OTHER TYPE OF LIABILITY TO THE COUNTERPARTY.



## DRAFTING CONSIDERATIONS (CONTINUED)

### Language Determines the Scope



#### ✓ Cap Time

Decide if the liability is limited or unlimited. Consider this: “We shall not be liable towards the Indemnified Party for any Claims that are notified on or after 4 years of the Indemnity Termination Date.” A tailor-made survival clause is an excellent way to protect the indemnifier.

#### ✓ Create Monetary Limitations

Consider the nature and extent of potential damage when establishing monetary caps. Will a third party be liable for damages, and if so, how much? What are the different risks, and how serious are they? Are these risks quantifiable?

Here is a good example of a monetary limitation, though you should consider it against the context of your situation: “The Vendor has no liability for any claim unless the damages exceed \$30,000.”





## DRAFTING CONSIDERATIONS (CONTINUED)

### Be Aware of the Side You're Representing



Pay attention to the priorities and liabilities of the party you're representing. This will help determine whether you should draft a one-sided or a mutual indemnity for your client.

### Familiarize, then draft.

When you use "hold harmless", the indemnity kicks in as soon as the indemnified party suffers a loss and the time period begins. "Make good" or "compensate" means indemnity becomes effective on the day when the indemnifying party is notified about the damage or loss. Examine party expectations regarding the time period to use apt language when drafting your clause.

#### Consider these questions:

- ✔ In this commercial relationship, which party will most likely be held liable?
- ✔ How much liability is transferred to the indemnifying party, and are they capable of handling it?
- ✔ Have you explored methods to limit or support their liability (e.g. insurance assistance)?

Reflect on these questions to appreciate your side of the contract.





## DRAFTING CONSIDERATIONS (CONTINUED)

### *Be Aware of the Side You're Representing*



#### **TIP**

- MAKE EFFORTS TO MITIGATE LOSSES AS THE INDEMNIFIED PARTY. USE LANGUAGE SUCH AS “BEST EFFORTS” OR “STANDARD OF CARE”. THE INDEMNIFIER SHOULD RECOMMEND SUCH A PROVISION.
- MAKE SURE TO INCLUDE TAX PAYMENTS AS A PART OF THE INDEMNITY AMOUNT.
- BE THOUGHTFUL ABOUT THE LANGUAGE YOU USE SINCE INDEMNITY CLAUSES ARE HEAVILY NEGOTIATED. ADOPT LANGUAGE THAT FAVORS GOOD LEGAL MECHANISMS LIKE ARBITRATION TO AVOID ENFORCEMENT CHALLENGES.
- UNDERSTAND PARTY OBLIGATIONS AS THEY DETERMINE THE TYPE, SCOPE, AND NATURE OF INDEMNITY CLAUSES.
- SEND AN IMMEDIATE NOTICE TO THE INDEMNIFIER IN CASE YOU USE THE “MAKE GOOD” LANGUAGE. INCLUDE THAT PAYMENT FOR INDEMNITY BECOMES DUE AS SOON AS THE NOTICE IS SENT AND THAT IT MUST BE MADE WITHIN A CERTAIN TIME FRAME.
- USE SEPARATE PROVISIONS FOR DIRECT AND INDIRECT LOSSES. ONE SPECIFIES AN INDEMNITY ARISING FROM A PARTY’S DEFAULT, WHILE THE OTHER ADDRESSES THIRD-PARTY CLAIMS.





# Define with Clarity

*While it's crucial to state what indemnity is, it's just as important to define what indemnity isn't. This will bring clarity that is often missed.*





## DEFINE WITH CLARITY



When defining damages, specify what's included in the word damage. When can something be qualified as damage? What are the nature, types, and consequences of this damage? And what is the extent (in monetary terms) of damage covered by the definition?

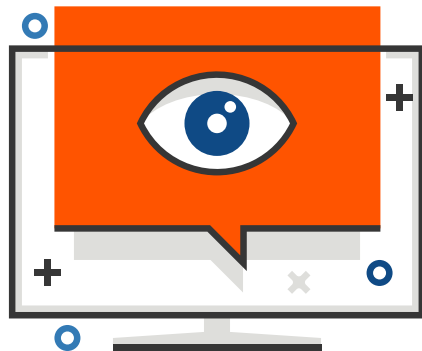
Avoid sloppy language to prevent misinterpretation. Draft better by having a clear intention behind adding a specific phrase.

Checklist for clarity:

- ✓ Look through the document for basic grammar errors.
- ✓ Use short sentences. 20-25 words per sentence should be your guideline.
- ✓ If you can express a phrase using one word, do it.
- ✓ Use active, not passive, voice.
- ✓ Don't use similar phrases many times just for impact. Use one phrase clearly.

*A personalized approach that takes extra effort is better than templated language that can be misconstrued.*





# Exploring Functionality

Let's look at two examples of company indemnity clauses from YouTube and LinkedIn to read between the lines, figure out the drafter's intentions, and comment on whether this clause is a good fit.





## EXPLORING FUNCTIONALITY

### YouTube



#### Indemnity

To the extent permitted by applicable law, you agree to defend, indemnify and hold harmless YouTube, its Affiliates, officers, directors, employees, and agents, from and against any and all claims, damages, obligations, losses, liabilities, costs or debt, and expenses (including but not limited to attorney’s fees) arising from: (i) your use of the Service; (ii) your violation of any term of these Terms of Service; (iii) your violation of any third party right, including without limitation any copyright, property, or privacy right; or (iv) any claim that your Content caused damage to a third party. This defense and indemnification obligation will survive this Agreement and your use of the Service.

#### Breakdown:

“To the extent permissible by law” means that they recognize there may be limitations on how indemnity is provided. It goes on to protect YouTube and all of its partners from all types of liabilities, making it a broad clause. It covers all legal costs and expenses apart from attorney fees. It also discusses how indemnity would kick in and covers many bases. It places the entire

burden of liability on the user and the creator using the app. Finally, it states that this obligation will survive the agreement, which is a good practice. There’s no time limit or monetary cap in this clause, shifting complete liability on the users and creators. This clause could be drafted better if it included those things.





## EXPLORING FUNCTIONALITY

LinkedIn



### 4.2 Exclusion of Liability

These are the limits of legal liability we may have to you.

To the fullest extent permitted by law (and unless LinkedIn has entered into a separate written agreement that overrides this contract), LinkedIn, including its affiliates, will not be liable in connection with this contract for lost profits or lost business opportunities, reputation (e.g., offensive or defamatory statements), loss of data (e.g., downtime or loss, use of, or changes to, your information or content) or any indirect, incidental, consequential, special or punitive damages.

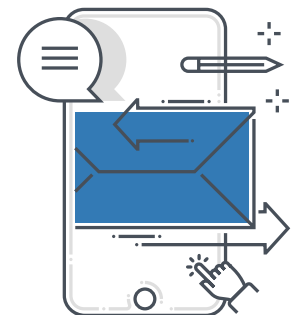
LinkedIn and its affiliates will not be liable to you in connection with this contract for any amount that exceeds (a) the total fees paid or payable by you to LinkedIn for the services during the term of this contract, if any, or (b) US \$1000.



### Breakdown:

LinkedIn's indemnity clause has a condition that reserves the right to not be held liable if another contract comes into play. In the event of a dispute, this condition necessitates a more thorough examination. They also mention platform-specific conditions for which they will not be liable, which is a clear indication of excellent drafting. This clause is a good example of a monetary cap. It was drafted keeping in mind the rates at which LinkedIn offers its paid services, and a calculated liability they're willing to pay.

LinkedIn and YouTube are both social media companies, yet their indemnity terms are very distinct. This is proof that drafting clauses and contracts with client-specific language is a useful practice.





## Key Takeaways

*Be Scope Conscious*

*"Make it happen" language*

*Careful Review*



## KEY TAKEAWAYS



**1**

**Be Scope Conscious**

The scope of indemnity determines the obligations of the indemnifier and the rights of the indemnified for the future. Make an informed decision. There's a lot at stake.

**2**

**"Make it happen" language**

Lawyers adore exhaustive language that covers all possible consequences. As important as it is to protect your client's interests, it's pointless unless the deal closes. Balancing out the two is vital.

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*Draft a clause that adheres to party preferences and intends to avoid a dispute.*

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**3**

**Careful Review**

A glance isn't a review. As an exercise, you can select a phrase from an indemnity clause you drafted, and comment why you included it (just for your reference). Being aware of your explanation will allow you to assess if it makes sense.



# Final Thoughts

*Handle indemnities with extra caution!*



## FINAL THOUGHTS



To become an effective drafter, you must work in tandem with client requirements rather than what is generally included. Instead of customizing a completely different indemnity clause from a different contract, use the current contract to understand the type of indemnity clause to write up.

If you're a fan of using provisions from templates, then make intelligent context-based tweaks. If you don't, you're putting your client at risk. This mini-guide should help you draft better indemnity clauses.



### ONE FINAL NOTE

While incorporating the fundamental elements of an indemnity clause, keep the drafting considerations in mind to carve a path towards robust clauses that are risk-free, reliable, and relevant.



## ABOUT

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Samridhi Jain is a legal content writer and contracts enthusiast. She helps law firms, lawyers, and legal SaaS companies with their content requirements.

She is inclined towards legal design, commercial and business laws, business development, entrepreneurship, writing, and content marketing. Samridhi loves learning about different areas and uses that to her advantage by cross-applying her skills. Having started early and jumped into freelancing, she now works with numerous clients from various jurisdictions including the US, UK, and India.

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Samridhi interviews lawyers from around the world on her Instagram page and shares her law school journey as well. She also loves simplifying contracts and legal concepts through digestible designs.

YOU CAN REACH OUT TO HER ON:



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