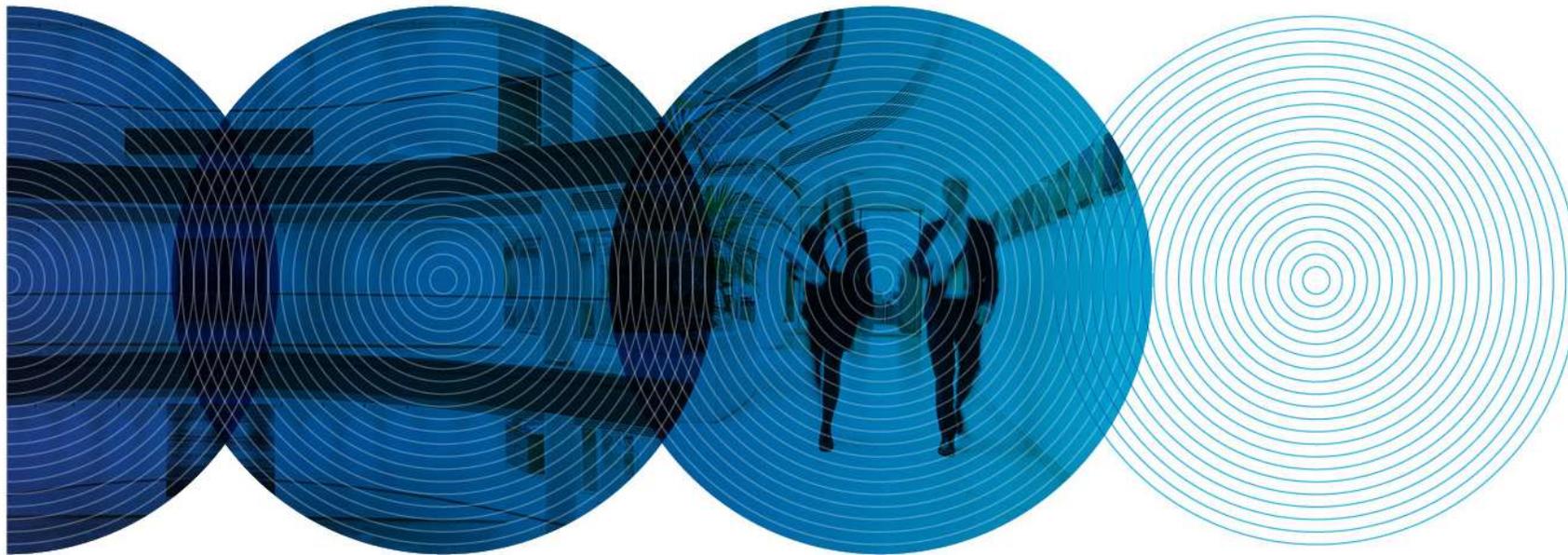


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# Indemnity Clauses

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# Introduction

**“How do you use the legal wriggle room surrounding indemnity clauses, including limitation periods and the level of recoverable losses, to secure an advantage in a dispute?”**

- What is an Indemnity:
  - Types of Indemnities;
  - Types of losses which may be indemnified.
- Negotiating an Indemnity Clause:
  - Exclusion Clauses;
  - What are the limitations on an indemnity.
- Practical Examples.

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# What is an Indemnity?

- There are no indemnities implied into services contracts in Irish law.
- Contractual promise by one party to another to pay money on the occurrence of a specified event.
- Allocates risk in a similar way to a warranty or a guarantee but the losses recoverable are different.
- Primary obligation - An indemnity will typically be triggered by losses being incurred, without the need to prove any "fault". This can also avoid rules around causation, which can otherwise make recovery more problematic.
- Triggered on the occurrence of the specified event irrespective of any fault on the part of the party giving the indemnity.

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# Indemnities in a Construction Context

- Construction Contracts
- A contractor will typically indemnify an employer with respect to:
  - Loss of or damage to property;
  - Death, personal injury, damage to third party property;
  - Breach of intellectual property rights (if design and build).

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## Indemnities in a Construction Context (cont.)

- Licence for Works
- A tenant will typically indemnify a landlord with respect to fit-out works being constructed:
  - Damage to the demised property;
  - Breach of planning or other consents required for the fit-out works;
  - Death, personal injury, damage to third party property.

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# Interpreting an Indemnity Clause

- The law on the rules of interpretation will be used to consider the extent of the indemnity provision based on the express wording used by the parties.
  - Law Society of Ireland v The Motor Insurers' Bureau of Ireland [2017] IESC 31 - contextual approach to interpretation
  - Dunnes Stores Unlimited Company v Dafora Unlimited Company [2022] IEHC 342 - if "*there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other*"

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# Interpreting an Indemnity Clause

- Given the recent focus in the courts on the express wording used, it is extremely important for an indemnity clause to be drafted carefully and to consider how they might work in practice.
- Some practical questions to consider when either drafting or considering what is covered by indemnity clause:
  - What is the appropriate trigger event?
  - What is the appropriate period the indemnity should cover?
  - What types of losses are covered?
  - Are any losses excluded?
  - How does the indemnity interact with other provisions in the contract?
  - When should the indemnity come into force?
  - What is required to satisfy the indemnity clause?

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## What is the trigger event?

- Indemnity provisions may provide one of three types of protections that dictate when the claim accrues.
- Accrual of Indemnity Against Costs and Damages
- Certain indemnity provisions apply to “losses,” “expenses,” “damages,” “costs,” and similar terms intended to convey that the owner has suffered out-of-pocket financial harm. With respect to this type of indemnity, the owner’s claim accrues the moment that it suffers the loss, i.e. makes payment to a third party. For example, if structural defects in the contractor’s work lead the owner to hire an investigative engineering consultant to provide an opinion on the necessary repair measures, the owner’s claim for indemnity to those costs accrues at the moment the owner pays the engineering consultant. The same is true for any other covered out-of-pocket costs or losses incurred by the owner; the claim accrues when payment has been made for those costs.

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## What is the trigger event?

- Accrual of Indemnity Against Claims and Liability
- Certain indemnity provisions obligate the contractor to “defend and hold harmless” against “claims,” “liabilities,” “awards,” and things of that nature. The duty to “defend” means that the contractor must pay for the costs of an owner’s legal defense. The duty to “hold harmless” means that the contractor must pay the judgment, settlement, or any other damages for which the owner is liable to a third party.

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## What is the trigger event?

- Accrual of Indemnity Claims Arising Out of a Promise to Perform
- The indemnity clause may contain language directing the contractor to take some future action in the event of a claim or damage. This type of indemnity claim most commonly arises in the context of the contractor's duty to defend. Where the indemnity provision expressly requires the contractor to take some specific action, the owner's contractual indemnity accrues immediately upon the contractor's failure to perform that action without valid justification.
- Contractual indemnity claims may accrue on different dates, depending on the nature of the indemnity and the language of the indemnity clause.

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# What is the trigger event?

- Practical Example
- Supreme Court case of Wood v Capita Insurance Services [2017] AC 1173.
- The case turned on the interpretation of an indemnity in a share purchase agreement, which read as follows:
  - "The Sellers undertake to pay to the Buyer an amount equal to the amount which would be required to indemnify the Buyer against all actions ... losses, claims, damages ... expenses and liabilities suffered or incurred, and all fines, compensation or remedial action or payments imposed on ... the Company following and arising out of claims or complaints registered with the FSA ... against the Company ... and which relate to the period prior to the Completion Date pertaining to any mis-selling or suspected mis-selling of any ... insurance related product ..."
- The question was whether the indemnifying party (Mr Wood as the seller) was required to indemnify Capita (as the purchaser) where there had been a loss "pertaining to ... mis-selling or suspected mis-selling of ... insurance products" but the claim being made did not arise out of "claims or complaints registered with the FSA" but arose as the result of an internal investigation.

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# What is the trigger event?

- Practical Example (continued)
- The court read the clause as follows:
  - "The Sellers undertake to pay to the Buyer an amount equal to the amount which would be required to indemnify the Buyer against **(1)** all actions ... losses, claims, damages ... expenses and liabilities suffered or incurred, and **(2)** all fines, compensation or remedial action or payments imposed on ... the Company **(A)** following and arising out of claims or complaints registered with the FSA ... against the Company ... **(B)** and which relate to the period prior to the Completion Date pertaining to any mis-selling or suspected mis-selling of any ... insurance related product ..."
- The critical distinction between the constructions presented by the two parties was whether:
  - (A) qualified both (1) and (2), in which case the indemnity would only apply if the loss arose from an FSA claim or complaint; or
  - (A) qualified part (2) only, in which case the indemnity would apply whether or not the loss arose from an FSA claim.
- The Supreme Court preferred the first interpretation: the words in (A) qualified both (1) and (2), and (1) could not be read as an independent trigger. Given that no claims or complaints had been registered with the FSA, the indemnity therefore did not apply.

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## What is the limitation period for enforcing an indemnity?

- The limitation period for an indemnity claim will not start to run until the date that the indemnified loss is established. This is because the trigger for a claim under an indemnity will be the suffering of loss that is covered by the indemnity.
- There is very little case law on this point in Ireland the case law in England and Wales is not consistent.
- There is an argument in England and Wales that including the words "on demand" means that the indemnified party may have a cause of action from when a demand is made by it, not from when the indemnifying party fails to make good on the indemnity.

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## Types of Losses that may be indemnified

- Exclude Indirect Losses?
- Direct Losses v. Indirect Losses (Hadley v. Baxendale)
  - Direct loss – recoverable losses which could reasonably be considered to arise naturally from a breach or could reasonably be supposed to have been contemplated by the parties at the time of the contract.
  - Indirect loss – losses which do not naturally result from a breach and are not recoverable unless the defaulting party had special knowledge of the potential for such loss at the time of the contract.
- Is loss of profit / loss of use etc a Direct or an Indirect Loss?
  - e.g. construction of a hotel

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## Types of Losses that may be indemnified

- In *Capita v RFIB Group* [2015] EWCA Civ 1310, the Court of Appeal held that the use of the words "directly or indirectly" in an indemnity clause imported the *Hadley v Baxendale* test of remoteness into the clause. The indemnity was worded as follows:
  - "The Seller undertakes to indemnify ... the Buyer ... from any liabilities costs claims demands or expenses which [it] may suffer or incur arising directly or indirectly from ... any services or products supplied ... prior to the Transfer Date".
- The court ruled that including the words "or indirectly" made it clear that the indemnity provided the widest link allowed by law in establishing liability for the relevant conduct. It held that the wording covered liability for losses within the second limb of *Hadley v Baxendale*, but that it could not cover liability for losses which are more remote than the second limb.

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## What does “hold harmless” mean?

- The meaning of the phrase “hold harmless” has been discussed in a number of cases notably in the UK Supreme Court in *Farstad Supply v Enviroco* [2011] 1 WLR 921.
- The court held that including the words “hold harmless” in an express obligation to indemnify “contains within it by necessary implication an implied term not to sue”.
- Therefore, in the UK at least, if Party A indemnifies Party B and the indemnity includes the words “hold harmless”, Party B suffers loss which is included within the terms of the indemnity, Party B is partially responsible for the losses that it has suffered as a result of its own negligence or breach of contract, Party B can rely on the “hold harmless” language in the indemnity to defeat a claim by Party A for a contribution.

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## How does the indemnity interact with the other provisions of the Contract?

- Are indemnities subject to contractual limitations of liability (including caps)?
- If the limitation of liability clause limits "liability under this Agreement", this would seem to cover a claim under an indemnity clause in the absence of indemnity clauses being expressly excluded.
- Are payments made under the indemnity clause intended to use up an aggregate liability cap?

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# Questions?



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