Indemnity: What It is, Why You Need It, and How to Get It…

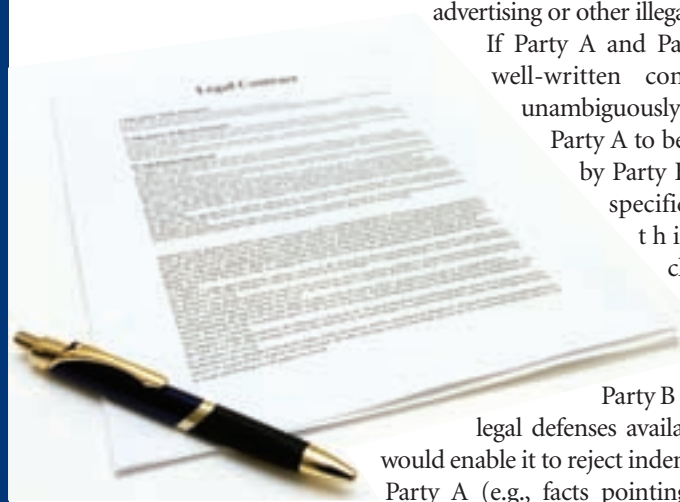
BY GREG SATER

"It's fine. I'm not worried, because I'm indemnified." How many times have you said that to yourself, but then had a fleeting moment of doubt, thinking: What does that actually mean? Am I really protected? Should I be worried?

I hear sufficient confusion about indemnity among marketers and vendors in our industry that I thought it would be useful to have a short "primer" on what it is, why you need it, and how to get it. I also thought it would be useful to recap some of the issues to consider when drafting an indemnity provision.

WHAT IS INDEMNIFICATION?

Although the fact patterns can vary, it usually is as follows: Party A has some sort of business relationship with Party B. For example, Party A is distributing Party B's product, and Party B is responsible for ensuring that it does not infringe on anyone else's intellectual property rights or injure anybody who uses it. Then, at some point, a third party comes along and sues everyone, including Party A, with regard to the product or its advertisements. For example, a competitor may allege patent, trademark or copyright infringement. Or a consumer may allege personal injuries. Maybe the FTC or another state or a federal agency alleges false advertising or other illegality.



If Party A and Party B have a well-written contract; if it unambiguously provides for Party A to be indemnified by Party B against that specific kind of third-party claim; and if, under the facts of the case, Party B does not have legal defenses available to it that would enable it to reject indemnification of Party A (e.g., facts pointing to Party A being at fault itself, partially or altogether, for the third party's claim and/or being in material breach of its contract with Party B); and if Party B is financially solvent enough to honor its contractual obligation, then Party B may be forced to pay for all of Party A's costs of defense in the third-party case, including its legal fees. Party B may also be forced to pay for any resulting monetary judgment the third party may win against Party A.

TAKING PRECAUTIONS

What lessons have been learned in the trenches of indemnity litigation?

First, understand that every contract is different and should be treated as such when it is being drafted. Each time you draft a new contract, you should consider what sort of third-party claims might arise from the venture or endeavor at hand, and then draft as comprehensive an indemnity provision as possible. In our industry, one such third-party claim is a product liability or personal injury claim relating to the design or manufacture of the product. Another is a claim of false or deceptive advertising, based on the TV commercial or advertising materials for the product. Such a claim can be brought either by a private plaintiff, a group of plaintiffs in a class action, a federal agency or state or local law enforcement agencies.

As between the parties to the contract, which party (Party A, Party B, both or neither) will be responsible for each of these kinds of third-party claims?

Another important potential third-party claim is that of intellectual property infringement, whether patent, trademark, trade dress, copyright, right of publicity or some other other. Which party will be responsible for that? Does it depend on whether it is a claim arising from the product (for which Party B may be most fairly held responsible) or from its advertising materials or cam-

paign (for which Party A may be most fairly held responsible)?

Finally, a party should always be indemnified for damages that arise from the other party's material breach of, or the failure of, any of its representations and warranties in the contract.

When well written, such clauses also should provide not only for indemnification against whatever monetary awards may need to be paid to a successful third-party claimant, but also for the payment of the legal fees and other costs of defense. It should discuss who will have the right to select the attorneys involved in the defense, who will have the right to control the defense and who will have the right to decide whether to settle with the future third-party claimant(s).

Another important point to remember is that indemnification clauses also should clearly state the "carve outs" from the indemnity obligation: the situations under which the indemnified party does *not* get its indemnity. If possible, it is best to try to customize each contract to the particular relationship.

Finally, are you not only indemnified but also insured? Most well-drafted contracts will provide for the indemnified party to be covered by an insurance policy purchased by the indemnifying party, and for the indemnified party to be named as an additional insured thereon. However, you must remember that the third-party claims against which you may be insured are not necessarily congruent with the third-party claims against which you are indemnified: the indemnity obligation usually will cover more types of claims than the insurance. So, in the never-ending quest for a shorter and simpler contract, do not make the mistake of foregoing an indemnity provision in your favor simply because you see that there's another provision making you an additional insured.

Also remember, an indemnity is only as good as the party promising it. If that party doesn't have the financial resources, or goes bankrupt, it is not worth the paper it is written on.

THE TACO BELL CASE

Indemnification disputes are frequently the subject of litigation in the advertising business. For a recent example, consider the case of *Taco Bell Corp. vs. TBWA Chiat/Day Inc., 552 F.3d 1137 (9th Cir. 2009)*.

Taco Bell used TBWA to create an advertising campaign. The parties had an agency agreement that included indemnification provisions. In it, TBWA agreed to defend, indemnify, and hold Taco Bell harmless from any third-party claims Taco Bell might be held liable for, based on or arising out of any materials created or produced by TBWA for Taco Bell, or arising from TBWA's fault or negligence in the performance of its obligations under the agency agreement.

However, another clause provided that Taco Bell would defend and indemnify and hold TBWA harmless from any third-party claims TBWA might be held liable for, based on or arising out of information or data supplied or proved by Taco Bell, or from Taco Bell's fault or negligence.

Language of this sort is common in contracts. But what if both sides might be responsible to some extent for the events that led to the third- party claim?

In the Taco Bell case, TBWA had developed an ad campaign centered upon a Chihuahua. It presented the idea for that campaign along with about 30 other ideas to Taco Bell. Taco Bell selected that idea and went with it. Taco Bell then was sued by someone who previously had been in talks with Taco Bell about a Chihuahua character.

The plaintiff sued Taco Bell for going forward with a Chihuahua-based ad campaign without them.

Because the third-party plaintiff's case against Taco Bell was based on the commercials that TBWA had created, as soon as Taco Bell lost the underlying case and suffered a $42 million judgment to that plaintiff, Taco Bell turned around and sued TBWA for indemnification.

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Despite the indemnity clause, however, the court ruled against Taco Bell, denying it the indemnification.

The court pointed out that Taco Bell itself had approved the Chihuahua character that TBWA had proposed to it, and had continued to approve each of the Chihuahua commercials thereafter made by TBWA, for broadcasting on television. So basically, despite the indemnity language in the contract favoring Taco Bell, Taco Bell's hands were not clean. It could not use the indemnity clause against its advertising agency, due to the way that that clause was worded in its agency agreement, and, applying that wording, due to its own involvement in the events leading to the third party's claims.

When considering your next contract, think about the different third-party claims that might arise because of something you do, or something the other party to your contract might do, and who should indemnify whom, for what—and how to clearly express these considerations. eR

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