

Software Contracts – Successfully Negotiating an Indemnification Section (Part 1 of 3)

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Indemnification is a very important provision in a software agreement. It transfers legal risk between contracting parties, and the indemnification provision acts like an insurance policy for future lawsuits where a contracting party is sued by a third-party to the contract. Because this provision is a risk transfer mechanism, it is crucial to understand it and to successfully negotiate it to prevent unwanted risk.

Before we jump into how to negotiate an indemnification provision, there are some basic definitions that need to be understood:

- An **Indemnitee** is a contracting party who is entitled to be indemnified.
- On the other hand, an **Indemnitor** promises to defend, indemnify, and hold harmless the Indemnitee against liability from a third person, or against loss resulting from liability.
- A **third-party** is a person or entity that is not a party to the original contract, but who sues one of the contracting parties.

So how does an indemnification provision operate? Typically, an indemnification provision is triggered when a third-party to the contract brings a claim against one of the contracting parties (i.e., contracting party vs. third-party claimant).

Very rarely, is it triggered when there is a direct party claim (i.e., contracting party vs. contracting party). At its core, an indemnification provision allows the party who is responsible for liability (the Indemnitee) to transfer his loss or liability to another party who will represent them in court (the Indemnitor), and pick up the litigation costs and liability from a third-party who bring a lawsuit against the Indemnitee.

One of the major pitfalls in negotiating an indemnification section is contained in the structure of the contract provision itself and the intent of the software licensor. Many contracts include boilerplate language, thus, contract negotiators must develop a systematic way to review the language and then develop a strategy to address the indemnification section for their side of the deal. To do this, the parties must first understand the risks involved with a particular software license and negotiate for the specific risk type.

The best way to put this into action is to review the indemnification section and put the language into more concrete roadmap to negotiate the contract by asking the following questions: (1) what are the licensor's objectives in the indemnification section, (2) what are licensee's objectives in the indemnification section, (3) what is a checklist of elements and questions that should be negotiated in a indemnification section, and (4) what is a general checklist of provisions that should be included in a indemnification section.

I will discuss each one of these questions in upcoming blogs.

Remember, an indemnification section is a specialized risk transfer section of a software contract. It is crucial to understand it and to successfully negotiate it to prevent unwanted risk. It is always important to seek advice from experienced legal counsel in order to understand all the risks

involved when negotiating these types of provisions in a software contract.