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**INDEMNITY UNVEILED: SECTION 124 AND 125 OF THE INDIAN
CONTRACT ACT, 1872**- Yashika Garg¹**ABSTRACT**

This paper examines the provisions of the Indian Contract Act of 1872 related to contracts of indemnity, explicitly focusing on Sections 124 and 125. It analyzes the essential elements of a contract of indemnity, highlights shortcomings in the text of the Act, and explores judicial pronouncements that have shaped the interpretation of indemnity contracts in India. The identified shortcomings include ambiguity in the definition, lack of specificity in determining damages, and the absence of provisions for third-party indemnity and breach consequences.

The paper suggests a creative approach to overcome these shortcomings, emphasizing the role of case law, model clauses, legislative reform, and the need to clarify the scope of indemnity. The proposed strategies are standardizing indemnity clauses, including mandatory provisions, providing guidelines, and addressing third-party beneficiaries. The conclusion underscores the importance of careful consideration before entering into indemnity contracts and the need for legal reforms to enhance clarity and fairness.

Keywords: Indian Contract Act, 1872; Contracts of Indemnity; Sections 124 and 125; Judicial Pronouncements; Shortcomings; Creative Approaches; Legislative Reform; Case Law; Model Clauses; Third-party Beneficiaries; Ambiguity; Standardization; Guidelines; Exclusion of Liability; Breach Consequences.

Central Government Act**The Indian Contract Act, 1872****According to Section 124 and Section 125 in The Indian Contract Act of 1872**

124. “*Contract of indemnity* defined.—A contract by which one party promises to save the other

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from loss caused to him by the promisor himself, or by the conduct of any other person, is called a contract of indemnity.”

125. *“Rights of indemnity holder when sued.—*The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor—The promisee in a contract of indemnity, acting within the scope of his authority, is entitled to recover from the promisor—

1. all damages which he may be compelled to pay in any suit in respect of any matter to which the promise to repay applies;
2. all costs which he may be compelled to pay in any such suit if, in bringing or defending it, he did not contradict the orders of the promisor and acted as it would have been prudent for him to work in the absence of any contract of indemnity, or if the promisor authorized him to bring or defend the suit;
3. all sums which he may have paid under the terms of any compromise of any such suit if the compromise was not contrary to the orders of the promisor and was one which it would have been prudent for the promisee to make in the absence of any contract of indemnity, or if the promisor authorized him to compromise the suit.”

ESSENTIAL ELEMENTS OF THE CONTRACT OF INDEMNITY

1. **Agreement** - The agreement is the foundation of the contract, and it must be based on a valid offer and acceptance. The offer is made by the indemnifier, who agrees to indemnify the indemnified against a specific event. The compensated accepts the offer by agreeing to the terms and conditions of the indemnity.
2. **Parties** - The contract of indemnity must have two parties - the indemnifier and the indemnified. The indemnifier is the party who agrees to indemnify the other party, while the indemnified is the party who is entitled to receive indemnity. The parties must have the legal capacity to enter into a contract.
3. **Loss or damage** - The contract of indemnity must be related to a loss or damage that may occur in the future. The loss or damage must be specified in the agreement, and the indemnifier must agree to compensate the indemnified for such loss or damage.
4. **Lawful consideration** - Consideration refers to the value exchanged between the

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parties. In a contract of indemnity, the consideration is the indemnity paid by the indemnifier to the indemnified. The consideration must be lawful, and it must have a monetary value.

5. **Mutual consent** - Both parties must agree to the indemnity terms and conditions, and the agreement must be entered into voluntarily. The consent must be free from coercion, fraud, or undue influence.
6. **Contingent event** - The loss or damage must be uncertain and may or may not occur. The indemnity contract is invalid if the loss or damage has already happened. The contingent event can be a specific event or a general event.
7. **No breach of contract** - If the indemnity contract violates the terms of another agreement, then it is not valid. For example, if the indemnity contract conflicts with an insurance policy, it is invalid. The parties must ensure that the indemnity contract does not conflict with any other agreements they have entered into.

SHORTCOMINGS IN THE TEXT OF THE CONTRACT OF INDEMNITY

1. **Ambiguity in the Definition** - The definition of indemnity under Section 124 of the Indian Contract Act, 1872, is broad and ambiguous. This definition can lead to confusion regarding the scope of the contract of indemnity. For instance, it is unclear whether the contract of indemnity covers only losses caused by the promisor's conduct or whether it also includes losses caused by the conduct of third parties.”
2. **Nature of damages, costs, or sums** - Section 125 does not provide any specific definition or formula for calculating damages, costs, or sums in the context of indemnity. This lack of clear guidance and numerical precision can lead to ambiguity and uncertainty, making it difficult for parties to assess their potential liability under an indemnity agreement. It can also result in inconsistent judgments by different courts, creating confusion and making it difficult to predict the outcome of disputes.
3. **Nature of Loss** - Section 124 does not explicitly mention the nature or extent of the loss that may be compensated under an indemnity contract. This would typically include any direct financial or monetary losses such as damage to property, loss of income or profits, or expenses incurred in rectifying the situation. It may also include indirect or consequential losses, such as the cost of emotional distress or psychological harm caused by the loss.

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4. **Lack of Specificity** - Section 125 of the Act states that the indemnifier is bound to compensate the indemnified party for all damages arising from the specified event. However, this provision does not provide any guidelines for determining the extent of damages that should be compensated. As a result, disputes may arise regarding the amount of compensation due under the contract of indemnity.
5. **No Provision for Exclusion of Liability** - This means that even if the indemnified party contributed to the loss or damage, the indemnifier is still bound to compensate them under the contract of indemnity. This can be particularly problematic in cases where the indemnified party's actions or omissions contributed significantly to the loss or damage. In such cases, the indemnifier may be unfairly burdened with the entire compensation amount.
6. **No provision for third-party indemnity** - The Act does not provide for third-party indemnity, a common practice in business transactions. This leaves businesses with limited legal protection and exposes them to risks.²
7. **No Provision for Partial Indemnity** - This means that if the indemnifier partially compensates the indemnified party for a loss, the indemnified party cannot claim the remaining amount under the contract of indemnity. Instead, they must file a separate claim for the remaining amount. This can lead to increased legal costs and time-consuming litigation. Moreover, it can be particularly challenging in cases where the loss or damage is ongoing, such as in the case of a breach of contract that continues over an extended period.
8. **No provision for breach of indemnity** - The Act does not provide for the consequences of a violation of indemnity. This leaves the indemnity holder with limited legal options in case of a breach, which can lead to financial losses.³

JUDICIAL PRONOUNCEMENT OF CONTRACT OF INDEMNITY UNDER INDIAN LAW

1. *Bank of Bihar Ltd. v. Damodar Prasad & Sons, 1969*⁴

In this case, the court held that a contract of indemnity is a promise by which one party promises to save the other from loss caused to him by the promisor himself or the conduct of any other person. It was also held that the indemnity holder is entitled to recover from the indemnifier all damages that he may be compelled to pay in any suit regarding any matter

²MULLA. (n.d.). The Indian Contract Act (13th ed.). LEXIS NEXIS

³SCC Online® | The Surest Way To Legal Research. (n.d.). Retrieved October 14, 2022, from <https://www.sconline.com/>

⁴Bank of Bihar Ltd. v. Damodar Prasad & Sons, 1969 AIR 297 1969 SCR (1) 620

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covered by the indemnity.

2. *UCO Bank v. Dipak Debbarma, 2013*⁵

In this case, the court held that an indemnity holder is entitled to recover all losses and expenses that he has been compelled to pay a third party regarding any matter covered by the indemnity. It was also held that the indemnity holder is entitled to claim interest on such losses and expenses from the date he paid them.

3. *United India Insurance Co. Ltd. v. Pushpalaya Printers, 2004*⁶

In this case, the court held that an indemnity holder cannot recover more than the actual loss suffered by him. It was also held that the indemnity holder must mitigate his loss and cannot retrieve any loss that could have been avoided by taking reasonable steps.

4. *Larsen & Toubro Limited v. Maharashtra State Electricity Board, 1995*⁷

In this case, the court held that the indemnity holder is entitled to recover not only the actual loss suffered by him but also the costs and expenses incurred by him in defending himself against any claim made by a third party. It was also held that the indemnity holder must mitigate his loss and cannot recover any loss that could have been avoided by taking reasonable steps.

5. *Indian Oil Corporation Ltd. v. Municipal Corporation of Greater Bombay, 1996*⁸

In this case, the court held that an indemnity holder is entitled to recover all losses he suffered, including any indirect or consequential losses, provided such losses are the natural and direct consequences of the act or omission covered by the indemnity. It was also held that the indemnity holder must mitigate his loss and cannot recover any loss that could have been avoided by taking reasonable steps.

CREATIVE APPROACH TO OVERCOME SHORTCOMINGS

1. **Case law:** One way to fill gaps in the statutory framework is through judicial interpretation of existing laws. Without clear guidance in the statute, courts can rely on precedents and case law to develop principles and standards for indemnity contracts. This can help clarify indemnity agreements' scope and the parties' rights and obligations.
2. **Model clauses:** Another approach is to develop model clauses or templates for indemnity

⁵ UCO Bank v. Dipak Debbarma, 2013

⁶United India Insurance Co. Ltd., Vs. Pushpalaya Printers, (2004) 3 SCC 694

⁷ Larsen & Toubro Limited v. Maharashtra State Electricity Board & Ors., 1995 (6) SCC 68

⁸Indian Oil Corporation Ltd. v. Municipal Corporation of Greater Bombay, (1997) 115 PLR 545

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contracts that can be used as a starting point for negotiations. Model clauses can help standardize contract language and promote consistency in how indemnity agreements are structured. They can also be a helpful reference point for parties unfamiliar with indemnity contract legal requirements.

3. **Legislative reform:** If gaps in the statutory framework are significant, it may be necessary to undertake legislative reform to update and modernize the law. This could involve clarifying the legal requirements for indemnity contracts, expanding the scope of indemnity coverage, or introducing new remedies or enforcement mechanisms to protect parties in the event of a breach.
4. **Clarify the scope of indemnity:** One way to fill gaps in the statutory framework is to clarify the scope of indemnity. This could include defining what types of losses or damages are covered under the contract and what types are not. This will help prevent disputes between parties over the interpretation of the contract.
5. **Standardize indemnity clauses:** Another approach is to standardize the language used to ensure they are unambiguous. This can help prevent misunderstandings and disputes between parties.
6. **Include mandatory provisions:** Some jurisdictions may benefit from compulsory provisions in contracts of indemnity. For example, they require that the indemnitor provide proof of insurance or financial responsibility to ensure that they have the means to pay for any losses or damages that may arise.
7. **Provide guidelines for indemnity contracts:** It may be helpful to provide guidelines or best practices to ensure they are fair and reasonable. This could include recommendations for the amount of indemnity to be delivered, the duration of the agreement, and other important terms and conditions.
8. **Address the issue of third-party beneficiaries:** The statutory framework should clarify whether third-party beneficiaries can enforce indemnity contracts. This is especially important in cases where a party enters into an indemnity contract to protect a third party.

CONCLUSION

The Indian Contract Act of 1872 provides for contracts of indemnity that allow one party to promise to save the other from loss caused by the promisor's conduct or any other person. However, certain shortcomings in the Act can lead to confusion and uncertainty, making it difficult for parties to assess their potential liability under an indemnity agreement.

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The ambiguity in the definition of indemnity, lack of specificity regarding the nature of damages, costs, or sums, lack of specific guidelines for determining the extent of damages to be compensated, and the absence of provisions for exclusion of liability are some of the issues that need to be addressed.

Parties must ensure that the indemnity contract does not violate the terms of any other agreements they have entered into. Additionally, they should carefully consider the potential risks and liabilities associated with the contract of indemnity before entering into it.



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