

What are the golden
rules for ensuring
that caps on liability
are (1) robust and (2)
enforceable?

Colin Fraser

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What will we cover today?

Liability Caps: the basics:

- Why?
- What?
- Where
- How much?

Trickier issues around enforceability:

- Unfair Contract Terms Act
- LDs
- Interpretation

1. Liability Caps: the basics

Why limit liability?

What is being limited?

- Overall exposure; and/or
- Liability for specific types of exposure e.g consequential /indirect loss, delay (LDs).
 - Be careful: loss of profit is not necessarily indirect loss
 - A clause which excluded “indirect special or consequential loss, howsoever arising, (including but not limited to loss of anticipated profits or data)” only covered loss of profit which could be said to be “indirect, special or consequential” (*Pegler v Wang, 2000*).
- “Each and every” claim or “in the aggregate”?

What is being limited?

- Remedies
 - Use of exclusive remedy provisions (common in PPP/PFI type contracts)
 - Exclude right to claim damages for breach at common law
- Notice requirements
 - for example in relation to EOT or loss & expense claims, can operate as exclusion or limitation provisions
- Common carve-outs from caps:
 - Death/Personal Injury due to negligence
 - Fraud
 - Wilful Misconduct or Gross Negligence (something more fundamental than a failure to exercise reasonable skill and care)
 - Losses on termination due to default

Where?

- Project Agreements
- Construction contracts
- Design appointments
- Collateral Warranties

How much?

- Fixed monetary cap or percentage of the contract sum: consider whether original contract sum or contract sum as varied.
- Pegged to level of insurance cover – amount (£) or basis (each and every or in the aggregate)? If amount only can be unsatisfactory.
- Different levels of cap for different types of loss e.g may be much lower limit in relation to losses linked to site investigation.
- Use of Net Contribution Clauses
 - Loss attributable to two parties; client can recover 100% of loss from one of those parties
 - NCC changes that: the consultant will only be liable for its share of the loss

Default positions in the standard form contracts (1)

FIDIC Yellow Book 2017

- Liability is capped at the value of the contract
- Exclusions apply to all consequential losses, and specifically:
 - loss of profit
 - loss of contract
- Carve-outs apply to specific areas:
 - fraud,
 - gross negligence
 - deliberate default
 - reckless misconduct

Default positions in the standard form contracts (2)

NEC3/4 Engineering and Construction Contract (Option X18)

- Parties may agree overall cumulative cap
- Separate caps may be agreed for:
 - damage to Employer's property
 - liquidated damages
 - design defects

JCT Standard Building Contract 2011/2016

- No overall cap
- Specific caps apply to consequential losses

2. The “tricky” issues

Unfair Contract Terms Act 1977 (1)

- UCTA typically applies to consumer contracts, but also applies to business to business contracts where the contract is based on a party's standard terms.
- If a party seeks to apply limitations of liability through its **standard terms**, that party must establish that the clause is reasonable
 - A clause is *“fair and reasonable having regard to the circumstances which were or ought reasonably to have been known to or in the contemplation of the parties when the contract was made”*
- How does a clause pass the “reasonableness” test?
 - What is the relationship between the liability cap and the contract price?
 - What was the relative bargaining position of the two parties?
 - Whether the client knew or ought reasonably to have known about the existence of the term

UCTA – the reasonableness test

Example one: REASONABLE?

- Sub-contract price £250,000
- Required to maintain insurance cover of £1m
- BUT sub-contractor's liability limited to the sub-contract price

Example two: REASONABLE?

- Sub-contract for ground compaction and piling work on basis of sub-contractor's standard Ts & Cs
- Claims for defects barred unless notified within 28 days of appearance and within a year of completion

Example three: REASONABLE?

- Contract price was £7.5k
- Standard terms of a specialist fire contractor contained wide ranging exclusion clause
- Liability would have been accepted if the employer had agreed to pay for insurance to cover the risk

Liquidated Damages

- The contract breaker's liability is limited to the amount of the LDs.
- Most common ground for challenging LDs is that they represent a **penalty**.
- **Test prior to 2015:** were the LDs a genuine pre-estimate of loss
- **Post 2015** Supreme Court case of *Cavendish Square Holding v El Makdessi*
:
 - Re-stated the test as:
“...whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker which is out of all proportion to any legitimate interest of the party in the enforcement of the primary obligation”

Interpretation of Limitation Clauses

- Limitation clauses were traditionally construed against the party seeking to rely upon them (*contra proferentem*).
- Therefore became common practice to expressly exclude liability for own negligence on basis that, absent express wording to that effect, it was unlikely a clause would be construed as excluding liability for negligence.
- **Change in approach: move away from that traditional stance:** unanimous decision of the Court of Appeal, *Persimmon Homes v Ove Arup* 2017

Interpretation of Limitation Clauses

- ***“In relation to commercial contracts, negotiated between parties of equal bargaining power, that rule now has a very limited role....In major construction contracts the parties commonly agree how they will allocate risks between themselves...Exemption clauses are part of the contractual apparatus for distributing risk. There is no need to approach such clauses with horror or with a mindset determined to cut them down.”*** (LJ Jackson)
- HOWEVER despite the move away from the CP rule, it remains good practice where negligence is concerned to exclude liability for negligence EXPRESSLY. Don't leave it up to chance.

Questions

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