Article Information

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Webinar Q&As: 2024 'Clause & Effect' Series | Navigating Contractual Risks: Limitation of Liability, Warranties, and Consequential Losses

Piper Alderman provides answers in response to the questions received during our 2024 'Clause & Effect' – Navigating Contractual Risks: Limitation of Liability, Warranties, and Consequential Losses 8 October 2024.

Thank you to everyone who participated in our webinar on Limitation of Liability and Consequential Loss. There were a number of questions that we did not have time to answer, so we have included the answers here. Where it made sense, we have combined questions with a similar theme.

Negotiating:

Question: What practical advice do you have for trying to negotiate (or live with) very one-sided limitations of liability or indemnities when contracting with a larger party such as a global provider or a government authority?

Unfortunately this is sometimes the "cost of doing business". Some options are:

- seeking to better understand the underlying risks that the counterparty is trying to mitigate, and then tailoring the clauses to reflect those risks;
- seeking to make some qualifications, e.g., that the indemnity from you does not apply to the extent that the loss in question was caused by an act or omission of the counterparty;
- if the counterparty is limiting their liability in an extreme way, seeking to increase the monetary cap and/or seeking to carve out (or have a more generous cap) for liability or loss caused by wilful misconduct or gross negligence.

Interpretation

Question: In what external circumstances (i.e. not in the contract) will the courts find that a contract is ambiguous? Is it when both sides' interpretations are reasonable?

If the court forms the view that the black-and-white words of the contract could have two different meanings, it could be due to the court accepting that the differing interpretations put forward by the parties are equally valid.

The general rule is that where ambiguity exists, the court will interpret the contract to give rise to the commercial intent of the parties. To interpret the commercial intent, the court will also have regard to the surrounding circumstances known to the parties, and the purpose and object of the transaction (*Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 [40]).

The parol evidence rule prevents the admission of evidence outside of the contract unless it evidence of surrounding circumstances (i.e., mutually known facts). Mason J explained in *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337 at 352 that the purpose of the rule is to exclude evidence from varying or contradicting the written language of the contract. His Honour also clarified that the true rule is that surrounding circumstances are only admissible where an ambiguity in the contract exists.

Question: In McMahon Mining Services, would the court only have rewritten "or" to be interpreted as "of" with

the consent of the parties?

The court simply commented on the "minimally inadequate proof reading" and assumed that the editing would not be regarded as contentious.

Question: The "last shot" doctrine seems to have been displaced in UK law, whereas in Australia it appears we still favour "later in time" documents/amendments. What is the current position on clauses that intend to restrict how future documents (eg, work orders) can arise (ie, can they vary positions, even though the master terms under which they are created, forbid such action?)?

The UK decision in *TRW v Panasonic Industry Europe GmbH* [2021] EWHC 19 departed from the last shot doctrine because TRW physically signed Panasonic's contract that stipulated the terms of the contract '*shall apply exclusively to the entire business relation*'. Shortly after TRW provided a standard purchase order form which included their own terms and conditions. Despite firing the last shot, the court held that Panasonic's terms and conditions prevailed because TRW signed the contract which indicated acceptance. This showed that TRW expressly accepted Panasonic's terms and conditions, and thus, the last shot did not prevail.

The UK position has not been confirmed by Australian courts. However, the key takeaway from the decision is that the last shot doctrine is not solely concerned about the timing of documents/amendments. What is important is when the offer and acceptance takes place.

Question: Given profit can be direct or indirect loss, is it necessary to use "indirect profit" in the definition of consequential loss?

If "loss of profit" is included as an example of "consequential loss" then it will be regarded as consequential loss regardless of whether it occurred "directly" or "indirectly".

Question: Where the categories of consequential loss are preceded by the words "for example", does this change anything?

That will depend on context. Whether a category of loss that is not referenced as a specific example ends up being regarded as "consequential" will depend on the overall wording of the definition of consequential loss or of the relevant exclusion clause.

Question: Do the courts calculate the loss first before deciding whether it is direct or indirect loss? Should one not first decide what type of loss it is?

The two exercises overlap. The courts need to consider what is at stake as well as whether it should be awarded. Calculations of quantum would probably come in the first instance from the parties' own submissions and then the court would be deciding on how those losses are categorised, and then where they fit within the structure of the contract.

Question: Will consequential loss be defined by what is in the contract or what has been decided by the courts as the definition of consequential loss?

- The first place the court will look is at the words of the contract itself.
- In the absence of clear descriptions in the contract, the courts will then consider the principles such as those outlined in the Peerless case.

Question: Would drafting exclusions to a consequential loss clause effectively be interpreted as an attempt to define "direct" loss?

If you define consequential loss as "not including" certain categories of loss, then by necessary implication those categories of loss would be included the bucket of "direct" loss.

<u>Quantum and Extent of Limitation of Liability</u>

Question: Is there an industry expectation of say, multiple (say 2x) of invoiced amount in the past 12/24 months.

Yes. Different limits of liability are considered reasonable in different industries from time to time. For example, in contracts for certain types of professional services (eg: engineering design), liability for professional negligence is often limited to the value of available professional indemnity insurance. In contracts for the sale of certain types of goods, liability is often limited to the price of the item sold. Ultimately, the value of any limit will be negotiated and might take the form of:

- the contract value or a multiple of the contract value (eg: 1 to 3 times the contract value);
- a figure that aligns with the perceived risk and estimated potential damages caused by any contractual breach (e.g. contemplation of a wide-scale data breach); and
- where a contract provides for goods and/or services to be delivered over several years, capped annual limits.

Question: Where would a cap on liability of 10% sit with respect to unfair contract terms?

It will depend on context. For example, if a large project is being delivered in instalments, the cost of rectification of any particular "instalment" may be less than 10%, so that limitation may be reasonable. In other scenarios, particularly if the "unfair contracts" regime applies, it would probably be regarded as unreasonably burdensome on the smaller party without protecting a legitimate interest of the bigger party.

Question: Does a general limitation of liability clause work equally well as one that states individual heads of claims like in tort, equity, contract, negligence etc.?

If a defendant denies liability on the basis that there is a limitation in the contract, the defendant bears the burden of proving that the contract included a limitation and that, properly interpreted, the exclusion effectively applies to the particular form of legal liability claimed by the plaintiff.

Generally, all liability clauses, whether specific or general, should be drafted in clear language. Excluding liability for serious matters such as negligence requires explicit mention of the exclusion of liability. General drafting will not suffice in such instances.

In drafting limitation clauses for standard form contracts with "small business" counterparties, particular care must be made to ensure the clause is not an unfair contract term. Clauses that absolve all liability, no matter the circumstances, have been held to be unfair since they force the customer to assume the risk of non-performance in circumstances outside of their control (*ACCC v JJ Richards & Sons Pty Ltd*).

Question: Can a party cap, limit or exclude its liability for personal injury, death or property damage whether caused by the party's negligence or any other cause?

Yes. Clear words expressly excluding liability are necessary (*Thomas National Transport (Melbourne) Pty Ltd v May & Baker (Australia) Pty Ltd* (1966) 115 CLR 353, 376; *Davis v Pearce Parking Station Pty Ltd* (1954) 91 CLR 642, 649).

Question: Does "to the fullest extent permitted by law" effectively limit liability?

Courts have interpreted the phrase "to the fullest extent permitted by law" as creating an unlimited indemnity (in indemnity clauses), potentially creating 'a significant imbalance in the parties' rights and obligations under the contract' in contracts for consumers and small businesses (*ACCC v JJ Richards & Sons Pty Ltd* [2017] FCA 1224 [56(g)]). If used in a standard form contract, there is a real risk clauses drafted this broadly will be declared unfair under ACL s 23.

Question: What are some best practices for drafting limitation of liability clauses to make them as clear and enforceable as possible?

- Think about how to break up the narrative so that you do not have a long and rambling sentence, but instead use subclauses, each with their own number.
- Use examples where that may be helpful in clarifying what is or isn't contemplated as being consequential loss.
- Alternatively, where you feel that there is a risk of misunderstanding, use a phrase such as "for the avoidance of doubt" to further elaborate on what is or is not intended to be included.
- Where possible, give yourself a break from the document and come back later with fresh eyes or ask a colleague/trusted external advisor to take a look with fresh eyes.

<u>Insurance</u>

Question: Can liability be limited to an insured amount? Can liability be limited to an insured amount under a 'per claim' policy? Why do parties do this?

Yes, with clear drafting.

Parties usually do this to ensure potential liability – or potential types of liability, such as liability for personal injury etc – is covered by an appropriate insurance policy. This serves two primary purposes:

1. the amount payable by the wrongdoer will be limited to the deductable payable under the insurance policy; and
2. the innocent party achieves a higher level of certainty that loss or damage will be recovered (given insurance

policies are typically underwritten by others, limiting insolvency risk etc)

Question: Can amounts recoverable from insurance be excluded from a contractual limit of liability?

Yes, with clear drafting.

Question: Can a monetary cap on liability prejudice your insurance cover (eg: if a cap on another party's liability prejudices the insurer's ability to recover amounts paid to you under your insurance policy)?

Potentially. This is why it is prudent to have your insurance agent review significant contracts and confirm that proposed contract terms do not prejudice your insurance cover.

Australian Consumer Law

Question: Even if the contract is not ambiguous, won't the court still take into consideration (if applicable) the Australian consumer law including the Unfair Contract Terms Regime?

Yes. Even if the clear interpretation of the contract is that there is a limitation of liability, that limitation may be found to be void if it is included in standard form contract and would be regarded as unfair under the Unfair Contract Terms Regime. Similarly, a clear exclusion of liability for misleading and deceptive conduct will fall foul of the restriction on excluding liability under that provision.

Question: Under the Unfair Contract Terms Regime, would it assist to have a concession within the contract that the counterparty agrees that the liability limitation or exclusion is reasonably necessary?

Requiring the "weaker" party to agree that a clause was "reasonably necessary" would probably not change the position if objectively the clause was unfair. You might have a better outcome if you included an explanation as to why the clause was there.

Question: Can liability under the ACL be excluded?

Deeds or agreements imposing blanket exclusions on claims for misleading and deceptive conduct will most likely be found to be contrary to public policy and won't be enforced by the courts. There may be scope to limit exposure to ACL claims by including time limits within which ACL claims may be made: *Viterra Malt Pty Ltd v Cargill Australia Limited* [2023] VSCA 157; *Price v Spoor* [2021] HCA 20.

Question: Is there a cap on contract value to be caught by ACL?

Our webinar was directed to breaches of s 18 of the *Australian Consumer Law* through misleading or deceptive conduct. There is no cap on the contract value to which s 18 applies. However, other provisions of the ACL (e.g.: consumer guarantees) only apply to contracts below prescribed values.

Question: How long should the temporal clause provide for on ACL clauses?

As short a time frame as you can reasonably negotiate, noting that risk remains that a court might find a temporal limit invalid. (*Price v Spoor* (2021) 270 CLR 450 [117])

Question: If a clause excludes liability for breach of contract, negligence and under the ACL, and is found to be not enforceable under the ACL, will it still be upheld for any liability for breach of contract or negligence? Should there be a separate clause to limit liability under the ACL to ensure that limits on any liability for breach of contract or negligence are not prejudiced?

This will depend on the particular circumstances, the meaning and effect of any severance clause included in the relevant contract and application of the doctrine of severance. However, if liability arises under the ACL, it is likely any enforceable limit on liability for tortious or contractual claims will be of very cold comfort.

We look forward to connecting in future webinars.

Meanwhile, please reach out to us if you would like to explore any of these issues in more detail.