

The sky isn't the limit – recent judicial consideration of limitation clauses

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Limitation clauses serve a crucial role in commercial contracts. They ensure that a contracting party manages their liability and avoids the spectre of disproportionate claims being made against them. In two recent cases, the English Courts have had the opportunity to consider different aspects of such clauses: in one case, whether a clause extends to limit the right to recover a debt, and in the other, whether liability for fraud may be effectively excluded.

Costcutter Supermarkets Group Ltd v Vaish & Anor [2024] EWHC 152 (KB)

Background

Ameer and Pradeep Vaish (“**Vaish**”) entered into contracts with Costcutter, whereby Costcutter would supply goods for Vaish to sell. After Costcutter changed its supplier, the quality of service fell. Vaish decided to end their relationship with Costcutter, and moved their business to a rival chain. Costcutter asked Vaish to pay for the goods that they had received but not paid for. Vaish declined to pay because of a limitation clause in the agreements, and counterclaimed for damages arising from Costcutter’s alleged poor service.

The Limitation Clause

The agreements between Vaish and Costcutter provided that:

“... the total liability of either party shall in respect of all acts, omissions, events and occurrences whether arising out of any tortious act, breach of contract or statutory duty or otherwise arising in any particular Contract Year in no circumstances exceed a sum equal to five (5) times the Service Charge paid by the Retailer to the Consultant in respect of the Contract Year immediately prior to the Contract Year in which such claim was made”.

At first instance, the Court agreed with Vaish’s argument, that the clause above applied to Costcutter’s claims for payment in respect of the goods received because that claim “*arises out of a breach of contract ... or otherwise*”. Because no service charges had been paid in the preceding year, the Court held that Vaish’s liability was limited to 5 x £0 = £0.

Appeal to the TCC

Constable J, sitting in the TCC, did not accept the judgment of the first instance court. Of importance to Constable J was the distinction between an action for debt and an action for damages following breach of contract. In an action for debt, the court is simply enforcing the parties’ primary obligations. The obligation to pay damages arises as a result of breach of contract. It is a secondary obligation which comes into being after the breach of a primary obligation under a contract causing loss. In the present case, Costcutter did not need to show it had suffered a loss (although it probably had) – it was just seeking to enforce, directly, Vaish’s promise to pay for the goods.

Constable J found that the limitation clause was directed “*expressly to acts or omissions arising out of any tortious act, breach of contract or statutory duty*”. Costcutter’s action for a debt did not fall under any of these heads, as it was not based on a breach of contract. Nor would the words “*or otherwise*” come to the rescue – Constable J found that this was “*not sufficiently clear*” to exclude a claim to enforce a primary obligation to pay.

As well as finding that the language was not sufficiently clear, Constable J queried whether such an exclusion could “*... ever exist meaningfully in an effective contract*”. This is in line with Lord Wilberforce’s comments in *Suisse Atlantique* [1967] 1 AC 63, that “*One may safely say that the parties cannot, in a contract, have contemplated that the clause should have so wide an ambit as in effect to deprive one party’s stipulations of all contractual force; to do so would be to reduce the contract to a mere declaration of intent.*”

Innovate Pharmaceuticals Ltd v University of Portsmouth Higher Education Corporation **[2024] EWHC 35 (TCC)**

Background

Innovate Pharmaceuticals (“**IPL**”) entered into an agreement with the University of Portsmouth (“**UOP**”) whereby UOP would conduct research into the properties of a patented drug to treat brain tumours, led by the UOP’s Dr Richard Hill (the “**Contract**”).

However, after a scandal regarding a paper published by Dr Hill, IPL claimed that he had fraudulently misrepresented raw data from the research conducted. IPL sought to recover their estimated loss in value of the patent due to Dr Hill’s inaccuracies. Because of these allegations of dishonesty, IPL was able to argue that UOP’s liability was not limited by the limitation clause set out in the contract.

The Limitation Clause

Clause 11 of the Contract provided that:

“11.4 ... the University is not liable to the Funders because of any representation (unless fraudulent), or any warranty (express or implied), condition or other term, or any duty at common law, non-observance or non-performance of this Agreement, for:

any loss of profits, business, contracts, opportunity, goodwill, revenues, anticipated savings, expenses, costs or other similar loss; and/or
any indirect, special or consequential damages or losses (whether for loss of profits or otherwise).

11.5 The liability of a Party to another howsoever arising (including negligence) in respect of or attributable to any breach, non-observance or non-performance of this Agreement or any error or omission (except in the case of death or personal injury or fraudulent misrepresentation) shall be limited to £1 million.”

The judgment of the TCC

Because Roger Ter Haar KC, sitting as a judge in the TCC, ultimately concluded that Mr Hill had not been dishonest, he did not need to decide whether Clause 11 would still have applied if there had been fraud. However, his obiter comments on that point remain interesting.

It was common ground between the parties that a party cannot contract out of their fraud in inducing a contract – what is generally called fraudulent misrepresentation. The authority for this is a House of Lords decision, *HIH Casualty v Chase Manhattan Bank* [2003] UKHL 6. However, drawing on *Frans Maas (UK) Ltd* [2004] EWHC 1502, the Judge concluded that “... *whether a clause excludes liability for fraud in performance of a valid contract is a matter of construction of the commercial provisions and risk allocation*”. In other words, provided that a clause is clear that liability for fraud *in the performance* of a contract is covered by a limitation clause, there is no rule of principle invalidating such a provision.

In respect of Clause 11, the Judge considered that the words “*unless fraudulent*” applied only to “*any representation*”. This meant that the limitation clause would only not apply where it was a *representation* that was fraudulent, rather than a breach of warranty or term of the contract. The exclusion from the limitation clause would therefore only apply to a claim based “... *in the tort of deceit*” and “... *loss of profits caused by a breach of contract not involving a representation is excluded even if that breach was committed fraudulently*”.

While IPL argued that the clause should, in any event, be unenforceable under the Unfair Contract Terms Act 1977, which only allows a party to limit contractual liability insofar as the limiting term is reasonable, the Judge disagreed.

The supervening events were, he believed, very unlikely to have been in the contemplation of the parties when they contracted. He would therefore have been slow to strike down Clause 11 because of events outside of the parties’ contemplation. In any event, he considered the clause to be reasonable because: (i) the parties were of equal bargaining power; (ii) IPL was assisted by legally qualified persons in negotiations; (iii) IPL in fact negotiated a number of terms; and (iv) the amount of work UOP was performing, and their fee, was low – only £50,000. It was this last factor which appeared to carry the most weight, with the Judge commenting that “*The amount of the claim in this case (arguably in excess of £100 million) compared to the amount payable to UOP under the Agreement underlines the commercial reality, perhaps necessity, of the two clauses*”.

Comment

The Court’s decision in *Costcutter* highlights an important distinction between primary and secondary obligations. The Court will not permit an exclusion clause to hollow out a contract of any meaning. The decision in *Innovate*, on the other hand, demonstrates the Court’s desire to uphold freely negotiated commercial bargains, particularly where they are serving a valid commercial purpose. The concept that a party might limit their liability for fraud gives some pause for thought. However, the Judge’s *obiter* comments to that effect were made against the background of an agreement with a modest value, where the breaching party would not have assumed responsibility for losses way in excess of the value of the contract. It remains to be seen if this view finds judicial acceptance in other cases.