Welcome….

to the latest issue of *The Missing Piece*, the monthly legal bulletin from *In House Lawyer*. In House Lawyer is my individual and exclusive legal service with strong ideals and a bespoke approach.

In this issue I'll be reviewing a recent case which considered limitation of liablity in contracts; a topic I first touched upon in the third issue of *The Missing Piece*.

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The High Court has considered the meaning of common phrases in a clause excluding liability. However, contract interpretation depends in each case on the clause, the contract and the context. Another court could therefore reach a different conclusion, even on an identical clause, in a different context. In this case, the judge held that the clause excluded many kinds of loss except the loss that actually happened, which was the most predictable loss anyone might expect.

Background. When interpreting a contract, the judge should take into account not only the literal meaning of its terms, but also the parties' commercial intentions, so far as the courts can detect them from the contract and the evidence of circumstances in which it was made.

Clauses limiting liability are often interpreted restrictively. The primary objective of English judges in civil cases is to do justice, and their job normally involves awarding damages for breach of contract. They may perceive as unjust a clause that stops them awarding any damages for a breach of contract. A clause that seeks to exclude all liability may therefore fall victim to restrictive interpretation, and fail to exclude anything. This fact of life is supported by cases on contract interpretation suggesting that very clear language is needed to reduce the normal remedies for a breach of duty.

Decisions of a High Court judge at first instance are binding on lower courts, but not on another High Court judge or on any higher court. Even when a decision is binding, another judge may depart from it if the same question arises on materially different facts. In contract interpretation, the material facts include the clause, the contract, and the context in which the contract was made. A later court may therefore reach a different decision even on identical wording, if raised in the context of a different contract and a different situation. One judge will, however, pay attention to the views of another on a similar question, without being bound to reach the same conclusion.

Facts. The dispute in this case arose from a 3½-year shutdown of the Andrew oil and gas field in the North Sea. Scottish Power was the buyer under four almost identical contracts to buy gas from the Andrew field. During the shutdown, the seller failed to supply gas from this field, in breach of contract. Each contract contained a compensation mechanism, obliging the seller to supply gas at a reduced price once production re-started, to make up for the gas it failed to supply during the shutdown. The seller argued that this was the buyer's sole remedy for the breach. The buyer had bought gas to supply its needs, in place of the gas the seller should have delivered during the shutdown. The price of the replacement gas was higher than the contract price. The buyer claimed the difference as damages for breach of contract.

Limitation clause. The contracts included this clause, limiting liability:
"Save as expressly provided elsewhere in this Agreement, neither Party shall be liable to the other Party for any loss of use, profits, contracts, production or revenue or for business interruption howsoever caused and even where the same is caused by the negligence or breach of duty of the other Party."

Sole remedy clause. The contracts also included this clause, making the compensation mechanism the sole remedy for a failure to deliver gas (whether or not the failure was also a breach of contract):
"The delivery of Natural Gas at the Default Gas Price and the payment of the sums due in accordance with the provisions of Clause 16.4 shall be in full satisfaction and discharge of all rights, remedies and claims howsoever arising whether in contract or in tort or otherwise in law on the part of the Buyer against the Seller in respect of underdeliveries by the Seller under this Agreement, and save for the rights and remedies set out in Clauses 16.1 to 16.5 (inclusive) and any claims arising pursuant thereto, the Buyer shall have no right or remedy and shall not be entitled to make any claims in respect of any such underdelivery." (Clause 16 contained the compensation mechanism already described.)

Decision

The limitation clause. The judge's starting point was that, in the sale of goods, the basic normal measure of loss for non-delivery is the difference between the contract price and the market price. (The price actually paid for replacement goods is, strictly speaking, relevant only as evidence of the market price.) The judge did not think that the limitation clause was intended to exclude these basic, normal losses. To do so would make the limitation clause exclude all financial loss. The judge called this a perverse idea.

The judge thought that, instead, the limitation clause was meant to exclude various other losses, which had not occurred and were not claimed. In explaining this conclusion, the judge interpreted each item in the list of excluded losses:

- **Loss of profits.** Profits that might be lost if it was not possible to buy gas at market price to replace the contracted delivery, or loss of profits the buyer expected to make from using the gas that should have been delivered.
- **Loss of revenue.** Similar to loss of profits - so, revenue that might be lost if it was not possible to buy gas at market price to replace the contracted delivery, or loss of revenue the buyer expected to make from using the gas that should have been delivered.
- **Loss of contracts.** The value of contracts with other customers that might be cancelled, or not won, because of the supplier's failure to deliver.

- **Loss of production.** Loss caused if, because of the supplier's failure to deliver gas, the buyer could not use the gas to produce something else (for example, electricity).
- **Loss of use.** The loss of a profit or benefit the buyer expected to gain from using the gas the supplier had failed to supply.
- **Business interruption.** The judge did not explain this, except to say it "overlaps with other items and further indicates the general type of loss which the clause is concerned to exclude".

The sellers had suggested that the buyer's losses fell within the excluded categories of "loss of use" or "loss of production". On the judge's interpretation, they did not.

The sole remedy clause. However, the contract did provide some remedy for the buyer, in the contractual compensation for failing to supply gas. The judge found that this compensation was the sole remedy for a breach of contract falling within clause 16, as this breach did. The compensation clause therefore succeeded in excluding the buyer's claim for any further damages.

Comment. The lawyers drafting and reviewing the limitation clause may have supposed that it excluded all financial losses. If it was intended to do so, it failed, as often happens to a complete exclusion.
Drafting techniques that can help to defend an exclusion of liability against strict interpretation include:

- Don't just list types of excluded liability; add general words. In this contract, if the aim was to exclude all financial losses, the limitation clause might have said "neither Party is liable for any financial loss. Financial loss includes ...". It could then list the examples, ideally in separate sub-paragraphs. (The interpretation clause should also add here "but is not limited to").
- Recite facts supporting enforceability. If a total exclusion has been negotiated in exchange for a reduced price or other concessions, you can say so in the clause or in the background section at the front of the agreement. By recording in the contract the commercial justification for the clause, you reduce the scope for creative interpretation by the judge.

Finally, instead of a total exclusion, it sometimes makes sense to negotiate a cap on losses instead. This can offer, between no liability and full liability, a middle choice that may be more acceptable to a judge. In this case, the contractual compensation mechanism offered the judge this middle choice, allowing him to make the contract-breaker liable for an agreed sum and to give effect to the exclusion of other liability in the compensation clause. The judge's interpretation of common expressions in exclusion clauses is interesting but not binding or conclusive. It would have been possible to interpret the limitation clause in this case more literally and less restrictively. On that basis, the exclusion of "loss of profits" might have excluded the reduction to the claimant's profits caused by having to buy gas at market price rather than contract price. The principles of contract interpretation are so flexible that no form of wording can force an English judge to reach a result that he or she considers unjust.

THAT'S ALL FOR THIS MONTH…

If you have any queries, comments or request for future bulletins then get in touch, I would be delighted to talk to you or meet at your convenience.

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