

LIMITATION OF LIABILTY

The Ultimate Survival Strategy

By Rick Reed

As the engineer, architect, contractor, subcontractor, supplier, or other service provider involved in a multi-million dollar project, imagine that you have just learned the project has been destroyed, due to a flaw that might be your fault. Can your company survive a catastrophic liability hit?

Most construction industry service providers and most owners understand the concept behind a limitation of liability clause. Basically, the service provider wants to protect its assets against catastrophic liability exposure to the party with whom it contracts. Negotiating a limitation of liability obviously depends on the strength of the service provider's negotiating position, and negotiation strategy for such clauses is an art in and of itself.

But suppose you have gotten over that hurdle – the party with whom you are contracting to provide your services is willing to accept a contractual limitation of liability. What considerations go into making a limitation clause effective? Here are some of the points you need to consider:

Be sure the limitation of liability will cover all forms of liability, whether arising in contract, tort, strict liability or any other theory of law. Consider who needs to be protected by the limitation of liability. It should protect your affiliates, partners, members, stockholders, directors, officers, employees, and agents. If your subcontractors and suppliers may also insist on limiting their liability your limitation of liability clause may need to protect them also. Should your insurer be identified as one of the parties your limitation of liability protects?

Be sure the liability limitation clause's enforceability is not open to question. Courts typically don't require all capital lettering and that strong wording that makes the limitation apply even if you are negligent, but meeting these requirements anyway is wise.

You can only limit liability to the party with whom you are contracting. Don't forget that the rights of third parties are unaffected by your limitation clause. Keep in mind that some third parties may own an interest in the project. If they are not signing the contract with you, they somehow need to be bound to the limitation of liability provision. Speaking of third parties, realize that if you perform services for another entity at project site (e.g. helping out a subcontractor on the side), your limitation of liability may not apply to damage to the project that arises out of that extraneous work activity.

Resolve any conflicts between your limitation of liability clause and any other clause in the contract. Does the arbitration clause give the arbitrators unfettered authority to make an award without honoring the limitation of liability in the contract? Does an indemnity clause override the limitation of liability? Make sure the limitation of liability will survive the termination of the contract (regardless of who terminates and regardless of the reason for the termination). When seeking an agreement for a waiver of liability for the consequential damages of the party contracting your services, don't rely on a simple waiver that fails to define exactly what consequential damages are being waived. Many contract drafters fail to realize that consequential damages are only consequential if they were not in the contemplation of the parties' minds when they signed the contract, so the issue of whether lost revenue or profits was thought about at the time the contract was signed may be left open for a jury to decide.

Drafting limitations of liability can be tricky, but done properly these clauses may one day make the difference between life and death for your firm.

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