TECHNOLOGY AND INNOVATION

Overview of certain key considerations for limitation of liability clauses in B2B contracts

February 2021

This briefing provides a high level overview of certain key considerations in respect of the limitation of liability under Irish law governed B2B contracts. In particular, this paper focusses on the structure of liability caps; classification of certain categories of liability as irrecoverable; exclusion of certain categories of liability from the liability cap; and certain other key considerations (including the interaction between liability caps and indemnity clauses).

STRUCTURE OF LIABILITY CAPS

The structure and quantum of the liability cap(s) are usually the most heavily negotiated aspects of the liability clause in a B2B contract. This can at least in part be explained by the fact that market standard practice in respect of other aspects of the liability clause (e.g. irrecoverable losses and exclusions from the liability cap) is often well settled and understood by the contracting parties but ultimately, the structure and quantum of the liability cap(s) will frequently depend on the specifics of the proposed commercial arrangement between the parties and the respective bargaining position of each party. Nonetheless, there are common trends and approaches towards the structure and quantum of the liability cap(s) in B2B contracts which are considered further below.

Annual cap vs contract duration cap

A key consideration when structuring a liability cap is whether the cap will apply on an annual basis or across the life time of the contract. An annual cap will seek to limit a party's liability in each year of the contract to a specified amount while a contract duration cap will seek to limit a party's liability over the duration of the contract to a specified amount.

In practice, an annual cap is often preferred by a supplier because it enables the supplier to decrease its maximum liability in each contract year to a smaller amount (e.g. the amount of charges paid and payable in that contract year as opposed to the aggregate amount of all charges payable over the life-time of the contract). An annual cap can also have benefits for the customer as it provides the customer with certainty that it will be able to recover up to a specified amount from the supplier in each year. However, annual caps can also present some risks, particularly for the customer. For example, an annual cap could prevent a customer from recovering the full amount of a loss against the supplier where such amount exceeds the annual liability cap notwithstanding that the sum total of each annual liability cap over the duration of the contract is greater than the amount of the customer's loss.

It is, therefore, important for the contracting parties to carefully consider the merits of an annual cap and a contract duration cap when negotiating the liability clause in their B2B contract and settle on the most appropriate option in light of their shared and diverging commercial imperatives.

Quantum of liability cap(s)

The quantum of the monetary cap on liability in a B2B contract will often depend on the subject matter and value of the contract and the respective bargaining position of each of the contracting parties. However, the contracting parties also need to carefully consider how to structure the monetary value of the liability cap.

Two frequently used options are:

- tie the monetary value of the liability cap to the value of the charges and any other amounts that the customer pays under the contract; or
- set the monetary value of the liability cap as a specific monetary amount (e.g. €1 million).

One or multiple liability caps

Again, whether it is appropriate to include one or multiple liability caps is likely to depend on the nature of the proposed contractual arrangement between the contracting parties. For larger outsourcing or services agreements it is quite common for the parties to include multiple standalone liability caps to cover different categories of liability. The idea is that each of these caps will include a separate and distinct 'liability pot' which is available in respect of the types of liabilities that fall under that liability pot and that a claim against one liability pot will not act to reduce the amount available in respect of claims against another liability pot.

Please see below examples of some different types of liability caps:

a. Service Credits – where a supplier is required to provide services to meet specific service levels, it is common for the supplier to be obliged to pay service credits where it fails to meet such service levels. The parties may include a standalone cap in their agreement which places a cap on the supplier's liability for service credits.

b. Data Protection – it is becoming increasingly common for sophisticated services agreements to include a standalone cap in respect of breaches by one or both of the parties of their data protection obligations.

c. Property – the parties may wish to include a standalone cap in respect of the liability of one or both of the parties for property damage arising from a breach of contract.

d. General – the parties may include a 'general liability cap' which caps the liability for one or both of the parties in respect of all other liabilities which are not covered under separate specific liability caps.

IRRECOVERABLE LOSSES

In addition to including one or more caps on liability, it is common practice for a B2B contract to specify certain categories of loss that will not be recoverable by either party under the contract. A number of these categories of liability are considered below.

- Indirect Loss – in effect, the term "indirect loss" is primarily focussed on losses which are unforeseeable. If a loss is not the natural result of a breach of contract that occurs in the usual course of things, it will not be deemed foreseeable and will likely constitute an indirect loss.[1] An exclusion of liability for indirect loss is common practice in Irish law governed B2B contracts.
- Consequential Loss – the terms "*indirect loss*" and "*consequential loss*" are generally interpreted in Ireland as covering the same type of loss.
- Special Loss - Irish law governed B2B contracts do on occasion exclude liability for "special loss" but the meaning of this term under Irish contract law is often unclear. In practice, an Irish court may reasonably view this category of loss as the same as, or indistinguishable from, indirect/consequential loss.
- Exemplary Loss - these are losses awarded by a court in excess of a claimant's loss. They are intended to punish the defendant for egregious behaviour and are only available in limited circumstances such as where the defendant is guilty of oppressive behaviour or has calculated that the money to be made from his wrongdoing will probably exceed the damages payable.
- Loss of Profits - an exclusion of liability for loss of profits is generally intended to ensure that a party cannot recover profits that they would have received if the other party had not committed a breach of contract. Instead, each party may only recover costs and expenses that it actually incurs as a result the other party's breach of contract. An exclusion of liability for loss of revenues is also not uncommon in Irish law governed B2B contracts.

An important consideration when considering irrecoverable losses under a B2B contract is whether any exclusion for loss of profits, loss of revenue or any similar exclusions are intended only to exclude such losses to the extent that they are unforeseeable (i.e. indirect) or whether such losses are excluded regardless of whether or not they are foreseeable (e.g. indirect *and* direct loss of profits).

EXCLUSIONS FROM LIABILITY

It is standard practice in Irish law governed B2B contracts to specify those categories of liability in respect of which neither party can limit its liability. Indeed, Irish contract law dictates that contracting parties are not able to limit their liability in respect of certain prescribed types of liability. For example, Irish contract law prohibits a contracting party from limiting its liability in respect of: (i) death or personal injury arising from that party's negligence; (ii) fraud committed by that party; and (iii) failure by that party to give good title to goods. It is also common practice for the liability of each party in respect of wilful default (i.e. knowingly or recklessly committing a breach of contract) to be unlimited.

In some cases, a party may also seek to provide in the contract that the liability of the other party in an area of particular concern to the first party is unlimited. For example, a party may seek to provide that the other party's liability is unlimited for breaches by that other party of its confidentiality obligations. In some cases, a party may also seek to provide in the contract that the other party's liability under one or more indemnities granted by the other party under the contract is unlimited. An example of an indemnity for which a customer might seek unlimited liability from a supplier is an indemnity designed to protect the customer against liabilities suffered due to third party claims that the customer's use of goods/services supplied by the supplier breaches third party intellectual property rights.

OTHER KEY CONSIDERATIONS

We set out below a number of other key considerations to bear in mind when drafting and negotiating a liability clause.

Are indemnities subject to the liability cap?

This point was briefly touched on in paragraph 4 above and ultimately, the simple answer to this question is that it will depend on what the contract says. If the contract specifies that liability under indemnities is excluded from the liability cap(s), then the liability of a party in respect of claims made against an indemnity granted by that party under the contract will be unlimited. Conversely, if the contract includes a general limitation on each party's liability and does not specifically exclude liability in respect of indemnities from this general limitation, we think it is reasonable to conclude that any liability arising under an indemnity is likely to be subject to this limitation on liability. However, the most prudent approach is for the contracting party to explicitly address in the contract whether liability in respect of the indemnities granted under the contract is or is not

1 Hadley v Baxendale (1854) 9 Ex 341.

subject to the limitation on liability under the contract.

Insurance

The inclusion of contractual commitments to have in place relevant insurance policies can provide contractual assurance that a defaulting party will be able to pay liabilities incurred by the innocent party arising from this default. More specifically, such contractual commitments could require one or both of the parties to put in place specified types of insurance policies that are relevant to the contract in question (e.g. professional indemnity insurance, cyber liability insurance, employers' liability insurance) and prescribe a minimum level of cover for these insurance policies. This level of cover could be set at such a level so as to give a party comfort that the insured party has sufficient levels of insurance in place to cover any liabilities that the party may suffer under the contract as a result of the insured party's contractual breach.

Identifying recoverable losses

In addition to specifying certain categories of loss that are not recoverable under a contract, it can also be helpful for the contracting parties to identify specific types of loss that will be recoverable under the contract. This can help to remove ambiguity around the recoverability of a particular loss in the event of a claim by one party. One category of loss which is sometimes expressly identified in B2B contracts as recoverable is the additional cost of procuring and implementing replacements or alternatives for goods/services not supplied under the contract.

KEY CONTACTS

If you require advice or assistance on any matters discussed in this briefing, please contact any of the following.

Ian Duffy
Senior Associate
+353 1 920 2035
Ian.Duffy@arthurcox.com

Rob Corbet
Partner
+353 1 920 1211
rob.corbet@arthurcox.com

Colin Rooney
Partner
+353 1 920 1194
colin.rooney@arthurcox.com

Ciara Anderson
Associate
+1 415 829 4247
Ciara.Anderson@arthurcox.com

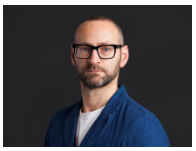
Rachel Benson
Professional Support Lawyer
+353 1 920 1435
rachel.benson@arthurcox.com

OUR TEAM

Rob Corbet
Partner
+353 1 920 1211
rob.corbet@arthurcox.com

Colin Rooney
Partner
+353 1 920 1194
colin.rooney@arthurcox.com

Olivia Mullooly
Partner
+353 1 920 1060
olivia.mullooly@arthurcox.com



Pearse Ryan
Consultant
+353 1 920 1180
pearse.ryan@arthurcox.com

Ian Duffy
Senior Associate
+353 1 920 2035
Ian.Duffy@arthurcox.com

Ciara Anderson
Associate
+1 415 829 4247
Ciara.Anderson@arthurcox.com

Caoimhe Stafford
Associate
+353 1 920 1328
caoimhe.stafford@arthurcox.com

Eoghan Clogher
Associate
+353 1 920 1405
Eoghan.Clogher@arthurcox.com

Aoife Coll
Associate
+353 1 920 1726
aoife.coll@arthurcox.com

Siobhán O'Shea
Associate
+353 1 920 1839
siobhan.oshea@arthurcox.com

Alison Peate
Associate
+353 1 920 1828
alison.peate@arthurcox.com

Rachel Benson
Professional Support Lawyer
+353 1 920 1435
rachel.benson@arthurcox.com