



**INTERNATIONAL COMPARISON -  
LIABILITY, INDEMNITIES &  
LIQUIDATED DAMAGES**

**Spring 2014**

**TRG law**

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## INTRODUCTION

We have undertaken a comparison between the position in England and Wales and various different jurisdictions in relation to certain aspects of liability, indemnities and liquidated damages and we asked a number of overseas lawyers some questions on these areas. Their responses are set out below with their contact details.

## ENGLAND AND WALES

### 1. What would an exclusion of consequential loss in a contract exclude?

It is well established that an exclusion of indirect and consequential loss does not exclude any loss which arises as a direct and natural consequence of the breach of contract. As such, by itself, it excludes relatively little.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

Not really in a B2B context. It is essential that the terms which contain the applicable limitation/exclusion clauses are sufficiently brought to the attention of the other contracting party before the contract is formed. Beyond that, English case law has from time to time historically mentioned possible additional requirements for clauses which are particularly unusual or onerous but, in reality, English courts accept that suppliers trade on standard terms and that these contain limitations and exclusions. There is an onus on customers to make themselves familiar with the terms of any offer/proposal and to raise objections if necessary otherwise they may well be deemed to have agreed to them.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

English law subjects limitation and exclusion clauses to a 'reasonableness' test - under 'UCTA' (the Unfair Contract Terms Act 1977) where they are contained in a supplier's standard written contract or where the clause purports to limit or exclude liability for negligence. In practice that means almost all limitations and exclusions are subject to this test. UCTA goes on to specify the criteria to be taken into account in assessing reasonableness.

#### b. Is there any ability to exclude liability for 'gross negligence'?

English law does not recognise a formal distinction between negligence and gross negligence. One can therefore exclude or limit liability for both subject always to the test of reasonableness referred to above.

#### c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?

Again, these statutory implied conditions can be excluded provided that doing so is regarded as satisfying the UCTA reasonableness test. Whether the exclusion of such implied obligations is regarded as reasonable will depend upon a number of factors but particularly what express warranties the supplier has given.

### 4. What happens if a limitation/exclusion fails any such legal control?

English Courts have no power to redraft an unreasonable financial limitation clause. The offending provision will simply be unenforceable. In most if not all cases the remainder of the contract will remain valid with the result that the supplier/service provider has potentially unlimited liability. The same applies to exclusions from particular types of liability. Depending upon the precise way in which the clause is drafted the Courts may be prepared to use a 'blue pencil' ie strike through and ignore particular offending exclusions whilst leaving the remainder intact and enforceable. For those reasons individual exclusions are typically drafted as standalone, independent sub-clauses.



## **5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Indemnities in respect of losses suffered by customers are becoming an increasingly common feature of contracts generally prepared by larger customers who are in a stronger bargaining position. The justification for such clauses is not so clear. It appears to be an attempt to avoid the well-established legal rules governing entitlement to damages, in particular the so called rules on 'causation' (the breach must be the effective cause of the damage) and 'remoteness' (the type of damage suffered must not be too remote in order to be recoverable. Essentially the damage must have been of a type which occurred naturally in the ordinary course or which ought reasonably to have been in the contemplation of the parties as a probable result of the breach) which limit what damages can be claimed in any particular situation. There is no particular necessity for such indemnities under English law. We have seen some suggestion that such clauses originated in jurisdictions which do not allow recovery of legal costs in the absence of such a provision.

## **6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

By liquidated damages (LDs) we mean pre-agreed payments or credits which are payable or claimable according to particular delays or levels of service below the contractually agreed levels. Under English law there is a longstanding and well known rule against 'penalties' (ie payments/credits which do not represent a reasonable pre-estimate of the likely level of losses which will be suffered as a result of the breach in question are unenforceable). However, in a B2B context this rule is now very rarely invoked since the threshold for assessing LDs/credits as penalties is set very high.

Essentially, to amount to a penalty the provision's primary purpose must be 'deterrence' rather than compensation. The LDs/credits must be set at such a level as to be 'extravagant and unconscionable almost amounting to oppression'. The one recent exception to this is clauses which provide for a remedy which does not vary in scale according to the extent of the breach. These single payments/credits which, for example, apply at the same level irrespective of whether the supplier is one day or two months late, have been declared as penalties and are therefore unenforceable.

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## **AUSTRALIA**

### **1. What would an exclusion of consequential loss in a contract exclude?**

Under Australian law 'consequential loss' has been used in many different ways in a wide variety of judgements with the outcome that it has lost its legal meaning and the concept has been largely replaced by the legal concept 'pure economic loss damages'. Colloquially, consequential loss is often taken to mean pure economic loss in the Australian environment. That being said, there is a real risk that when referring to consequential loss in a contract, the courts will take this to mean indirect losses that arise under the second limb of *Hadley v Baxendale* rather than direct losses occurring under the first limb of *Hadley v Baxendale*.

There is however, conflict in the decisions and in certain circumstances, consequential loss can be legally interpreted to mean pure economic loss damages. In all Australian jurisdictions, it has become increasingly important to be precise about the exclusion of loss and damages that is agreed between the parties by using words that achieve the desired outcome by their ordinary and natural meaning (following on from the decision on the interpretation of exclusion clauses of the High Court in *Darlington Futures v Delco*).

**2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

There are no special steps that are required in terms of prominence for exclusion clauses to be enforceable as a matter of contract law. The focus under Australian law is clarity of drafting within the context of the terms of the contract and the transaction it records. There are however a number of rules under the Australian Competition and Consumer Act (and related legislation) for the protection of consumers in transactions that may significantly affect the enforceability of exclusion clauses (and indemnities) in transactions with consumers.

**3. Are there any legal controls on limitation/exclusion clauses? In particular:**

**a) Is there any requirement of reasonableness?**

Under the Competition and Consumer Act (which houses the new Australian Consumer Law) there are a number of rights (known as consumer guarantees) given to consumers in transactions that cannot be excluded or affected by any exclusion clause (or any other indemnity or other provision). Also, the Australian Consumer Law has recently introduced an unfair contract terms regime in respect of standard form consumer contracts which renders unfair and voidable certain any unfair contractual terms. However, in the business to business environment there is effectively no requirement for reasonableness in an exclusion clause, although the exclusion clause will always be construed against the party seeking to rely upon it and will not be interpreted in a manner that results in an absurd outcome or in a way that defeats the giving of consideration under a contract.

**b) Is there any ability to exclude liability for 'gross negligence'?**

Generally, there is no concept of gross negligence in Australian law outside of particular legislative utilisations of the phrase. Accordingly, it is possible to exclude liability for gross negligence subject to clear language being used to achieve this outcome.

**c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

In consumer and domestic transactions there are a number of statutory guarantees and implied conditions that cannot be excluded. The relevant statutes often allow for a limited right of a supplier to limit liability where it is reasonable to do so such that the supplier can refund the purchase price or re-supply the good or service. However, these types of provisions do not apply in general commercial or business to business transactions in most instances.

**4. What happens if a limitation/exclusion fails any such legal control?**

If an exclusion clause fails the legal controls provided for consumer and domestic transactions, and the clause is not capable of interpretation in a way that satisfies those rules, the relevant exclusion provision will be unenforceable. In business to business transactions an exclusion clause that operates in a potentially absurd fashion will in most instances be interpreted in a way that makes it consistent with the objective of the contract unless to do so would create uncertainty, in which case the clause will be void for uncertainty.



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**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Under Australian law, indemnities that are designed to operate as exclusions of liability are at times called 'reverse indemnities'. Reverse indemnities are in most instances treated as being subject to all of the same rules as exclusion clauses. In the Australian contracting environment, indemnities are often sought for a wide variety of matters, including breach of contract. There does not appear to be any clear improvement to the entitlement to damages under an indemnity for breach of contract as opposed to damages for breach of contract except in the relatively narrow area of the recovery of legal costs. Under Australian law for an indemnity to affect the usual rules of causation and remoteness of damage, clear drafting is required in the indemnity.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

There are rules against the recovery of liquidated damages that constitute a penalty both at common law and at equity. Under Australian law a liquidated damages amount is taken to be a penalty where the amount of liquid damage recovery entitlement does not bear any relationship at all to the loss actually suffered. If liquidated damages are found to be a penalty at common law then the liquidated damage provision is unenforceable. Liquidated damages may also be seen to be penalties at equity where the liquidated sum is disproportionate to the loss. If a liquidated damage is found to be a penalty at equity a court may revise the amount of the liquidated damage recoverable to an amount which reasonably represents the loss actually suffered.

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## BELGIUM

**1. What would an exclusion of consequential loss in a contract exclude?**

Same as English law. Art 1150 of the Belgian civil code states that one can only be held liable for 'foreseeable damages' ('dommages prévisibles') and art 1151 of the Belgian civil code states that a party can only be held liable for damages resulting 'directly' from the performance of the agreement ("*qui est une suite immédiate et directe de l'inexécution de la convention*").

However quite a few interpretation questions may arise about these concepts, leading to uncertainty for both parties. It is therefore strongly recommended to clearly spell out what qualifies as direct or indirect damages by the parties.

The English concept of 'consequential damages' does not have an exact translation in Belgian law. It is likely to be assimilated to indirect damages. This again shows the need to provide clear definitions in the contract.

**2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

Definitely not required and could even be perceived as inappropriate.

If we do not face a contract that was duly negotiated by both parties and signed after amendments were made, but rather Ts&Cs were used which are standard and often in small print, the question may arise whether such Ts&Cs can be imposed on the customer. The service provider will have to show that these terms were communicated to the customer before it placed its order (in the alternative, the order form, signed by the customer, should indicate that it is based upon such Ts&Cs which the customer duly received). It will not be sufficient to have made them available on some website or to print them on the back of several invoices afterwards.

**3. Are there any legal controls on limitation/exclusion clauses? In particular:**

**a) Is there any requirement of reasonableness?**

Under Belgian law, limitations of liability B2B can be freely negotiated. Liability for 'wilful intent' cannot be excluded though. Liability for gross negligence can be validly excluded in a contract.

There is no requirement of 'reasonableness'.

The only limitation is that it is not allowed to completely undermine/dismantle the essence of the underlying essential contractual obligation: if it turns out that the contract is drafted in such a way, that it will eventually never be possible to hold the supplier liable for the services it renders (the object of the contract), then the clause is null and void (resulting in unlimited liability).

**b) Is there any ability to exclude liability for 'gross negligence'?**

There is no formal distinction between negligence and gross negligence and both can be excluded or limited. See point (a) above. Excluding only gross negligence may lead to debates about what gross negligence might mean (again this should be spelled out clearly in the contract to the maximum extent possible). This will be considered on a case by case basis.

**c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

No such statutory implied obligations in Belgium but if the purpose is obvious, or if it was clearly indicated upfront, it will be implied.

**4. What happens if a limitation/exclusion fails any such legal control?**

Judges may intervene to 'moderate' excessive or abusive indemnification/penalty clauses, if they consider that the indemnification resulting from its application was not, at the conclusion of the contract, aiming at compensating real losses but more like 'punishing' the other party (no 'indemnification' character). If they do so, the provision still stands (it is not null and void), but the judge will mitigate in fairness (reduce the outcome).

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

We face these clauses in contracts that are inspired by UK/US law (typically in M&A contracts, where indemnities are sought for specifically identified issues such as for example the possible consequences of an investigation, a known IP problem). It is not a familiar concept under Belgian law. The justification of such clauses is not so clear, and they should be negotiated together with the standard liability clauses.



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## 6. Is there any rule against liquidated damages which constitute a penalty being enforceable?

When contractual 'penalties' are negotiated, the agreed penalty is always due in case of non-performance, whereby the contracting party does not have the burden of proof of the impact it suffered from this non-performance (if any). We would rather call it a 'penalty', but the term 'liquidated damages' is also often used for contracts drafted in English.

In Belgian law there is also a longstanding and well known rule against 'penalties', as it is not allowed to have 'private enforcement' or 'punishment' by individuals. (In the early '90s lawyers even avoided using the word 'penalty' because it sounds like criminal law and has some law enforcement flavour to it).

A penalty clause is only valid in so far that upon contract signing the parties genuinely aimed at translating likely and foreseeable damages that could be anticipated where there is non-performance, into a lump sum indemnification. If the amount of the penalty is so high that the parties must have aimed at deterrence rather than at compensation for the potential likely damage which was reasonably expected to occur, the clause is null and void.

However, in a B2B context this rule is now very rarely invoked and penalties for SLAs are very common.

Since 1998 a court can reduce the impact of such clauses if it deems the clause to be abusive/excessive. The clause is not declared null and void but rather its impact is reduced to something considered 'reasonable'. The parties cannot exclude by contract the possibility for a judge to reduce the impact of the penalty if he thinks it is abusive/excessive.

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## CHINA

### 1. What would an exclusion of consequential loss in a contract exclude?

In China, the law does not expressly prohibit supporting a claim for indirect losses, however, in practice, it is quite hard to get any indirect losses to be upheld by the court. So, the position is the same as English law, it excludes little.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

In China, when excluding main liabilities in a standard contract, the law requires that the party providing the standard contract must remind the other party of the exclusion or limitation. However, the law is silent on how to remind the other party – there is no requirement to use bold type or capital letters, etc. However, in practice, bold type is often used as such a reminder. If it is not a standard contract, the law does not require such a reminder on the limitation or exclusion of liabilities, however, in practice, such limitations or exclusion clauses are often written in bold type.



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**3. Are there any legal controls on limitation/exclusion clauses? In particular:**

**a) Is there any requirement of reasonableness?**

No. However, Chinese laws prohibit the exclusion of liabilities for bodily injuries or death (safety issue) to or of the other party.

**b) Is there any ability to exclude liability for 'gross negligence'?**

Chinese laws do not recognize gross negligence or negligence as grounds to exclude liability.

**c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

Chinese laws do not have such implied obligations of fitness for a special purpose/satisfactory quality. However, Chinese law attaches an importance to the principle of 'Good Faith'. For instance, if I buy a car, though the law does not say what excellent quality this car must be, according to the 'Good Faith' principle, this car must basically run and be safe.

**4. What happens if a limitation/exclusion fails any such legal control?**

The same as in England, in China, such a limitation/exclusion will be unenforceable if it fails to meet the legal controls.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

No since the laws leave this to be agreed by the contractual parties. If such an indemnity clause is stipulated against a breach of contract, then the non-breaching party will seek to rely on it and typically such an indemnity can be supported according to what is stipulated in the contract.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

No since the laws also leave this to be agreed by the contractual parties. If liquidated damages in the nature of a penalty are stipulated in the contract, it is generally enforceable. However, when the liquidated damages are too high or too low, the other party may request the court to make a reasonable adjustment. Such adjustment is solely at the discretion of the judges since the Chinese laws are silent on how (in terms of scale or proportion) to make the adjustment.

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## **ECUADOR**

### **1. What would an exclusion of consequential loss in a contract exclude?**

According to Ecuadorian Law, damages are only categorized as emerging damages and loss of profits. As a consequence, under our legal system, there is no such category as consequential loss itself.

In light of the above, assuming that under emerging damages or loss of profits we include both direct and indirect damages (including consequential losses), only the agreement of excluding or condoning the future wilful misconduct is prohibited under the Ecuadorian Civil Code (art. 1481); as a result any other exclusion is acceptable.

### **2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

No, there are no special steps in business-to-business contracts. There are, on the other hand, restrictions in the case of consumer related issues, as the law states that the font used cannot be less than 10 points; that if certain clauses are written in a smaller font from the other clauses then such provisions are considered as not written; and, that it is forbidden to include reductions to text or documents that are not provided to the consumer at the time of executing the contract.

### **3. Are there any legal controls on limitation/exclusion clauses? In particular:**

#### **a) Is there any requirement of reasonableness?**

No, Ecuadorian Law does not include such legal controls - the parties are entitled to discuss these without limitation.

#### **b) Is there any ability to exclude liability for 'gross negligence'?**

Yes. According to the Ecuadorian Civil Code (Art. 29) gross negligence is equivalent to wilful misconduct. In consequence, under article 1481, it is prohibited to exclude liability for gross negligence (or wilful misconduct).

#### **c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

According to Ecuadorian laws (art. 1460 of the Civil Code), any contract implies obligations of three different kinds:

- a) those of the essence of the contract, that cannot be excluded otherwise the contract would not produce any effect or would turn into a different one;
- b) those of the nature of the contract, which arise from the specific type of contract without the need for any specific provision, and in consequence cannot be excluded either; and
- c) those accidental obligations that are to be included specifically by the parties, and consequently can also be excluded.

In our opinion, obligations of fitness for purpose can be categorized as obligations of the nature of the contract, and in consequence cannot be excluded (otherwise the contract would turn into a different one).

### **4. What happens if a limitation/exclusion fails any such legal control?**

If despite the limitations of the law, the parties do agree to include any particular limitation or exclusion of responsibility, such provision would be understood as being against the law and consequently 'morally impossible' under the terms of article 1477 of the Civil Code. This would lead to the fact that the clause would be considered as null and void due to an absence of lawful purpose.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

The Organic Law for Protection of the Customer states that it is a right pertaining to the customer to receive reparation or indemnification for any loss or damage suffered, as well as for deficiencies in the quality of goods or services (art. 4(8)). In light of that, not only does the law state that such rights cannot be waived, but also it is the same law (art. 43 (1)) that states that provisions excluding, limiting or extinguishing the responsibility of the provider are banned.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Compensation for damages includes consequential damages and lost profits. This applies when a party fails to comply with its principal obligation, having complied incorrectly or where there is a delayed failure.

Article 1551 of the Civil Code states that the parties are free to treat a penalty as a pre-liquidation of the damages arising from the failure to comply with the principal obligation, having complied incorrectly or where there is a delayed failure.

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## FRANCE

**1. What would an exclusion of consequential loss in a contract exclude?**

Breach of contract leads to compensation only for what was promised under the contract (can it be provided anyway, can money be paid instead?) and interest on overdue payments.

Any demand beyond the object of the contract itself is subject to negligence liability rules - article 1382 of the civil code - no matter what the parties have agreed in the contract.

Implementation of article 1382 of the civil code requires evidence of all of the three following elements: a wrongdoing, damage and a causality link (causation).

**2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

No. Terms of prominence only apply where consumers are parties to a contract (article L.132-1 of the consumption code). French law requires that terms be clear and precise in their meaning not shape or position (standard terms of business are entirely part of the contract, though terms generally submitted to the deal will prevail), and clauses are to be interpreted with respect to one another.

**3. Are there any legal controls on limitation/exclusion clauses?**

Both exclusion and limitation clauses are in principle admitted under contract law (but are null in relation to negligence liability/tort). Such clauses must have been brought to the parties' attention and

accepted by them. Yet many legal and case law exceptions exist (legal exceptions include notably transportation contracts, auctions, construction and sales between professionals and consumers).

**In particular:**

**a) Is there any requirement of reasonableness?**

(i) A limitation clause must not lead to depriving the contract of its purpose, of the main undertaking.

The French Supreme Court entered into the Chronopost ruling in 1996: the Supreme Court decided that the clause by which this fast service postal company was limiting its liability in case of late delivery (when clients were paying extra for fast/express delivery) was to be considered as not written (hence unenforceable.)

It should be noted that if such a clause is unenforceable, another legal set of rules may automatically apply, providing for other types of indemnification ceilings. In the Chronopost matter, legal public rules applying to ground transportation contracts applied and the parties were *de facto* bound by the ceilings for such rules.

(ii) Also, case law will not automatically allow limitation clauses which provide for derisory indemnities, which are in fact exclusion clauses. In such instances, limitation clauses are null when an exclusion clause would not have been permitted.

**b) Is there any ability to exclude liability for 'gross negligence'?**

Exclusion/limitation clauses are excluded in cases of wilful misrepresentation (as contracts must be executed in good faith) and gross negligence. Exclusion clauses apply to minor breaches.

**c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

Whether the exclusion of such implied obligations is regarded as reasonable will depend upon a number of factors but particularly what express warranties the supplier has given. Article 1386-15 of the civil code provides that clauses meant to exclude or limit liability caused by defective products are forbidden and considered 'not written'.

**4. What happens if a limitation/exclusion fails any such legal control?**

French courts have no power to redraft the contract's clauses. The offending provision will simply be unenforceable as it is considered as not written, and in most if not all cases the remainder of the contract will remain valid.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Article 1382 of the civil code applies (see above).

However it is important to underline that the same demand cannot be presented under both contract and tort rules.

Breach of contract will be treated in accordance with contractual liability rules and losses (other than default in the execution or late execution of the contract itself) will be presented under tort/negligence rules. But the line may not always be very clear.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

A penalty clause can be provided for in a contract. Its purpose is to set in advance the amount to be paid (or substitute an obligation in kind to be carried out) in case of failure of the party with the obligation.

The courts can both increase (if the amount is obviously derisory) and decrease (if the amount is obviously too high) the amount in the penalty clause.



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If the contract is declared null, then the penalty clause also falls. If the contract is terminated then the penalty clause survives.

The penalty clause cannot have the effect of derogating to a situation where exclusion of liability would be barred (for example: maritime transport of goods).

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## GERMANY

### 1. What would an exclusion of consequential loss in a contract exclude?

Under the German law on damages it is basically irrelevant if damage has occurred (directly) to the contractual object itself or (indirectly) to other legally protected goods. The crucial issue is the general obligation for compensation for all adequately caused consequences of the damaging event – irrespective of the question whether the damages are direct or indirect. Correspondingly, German law actually does not have a distinct differentiation between direct and indirect damages or direct/indirect and consequential damages nor a legal definition of these terms.

In contracts, the term consequential damage or consequential loss is understood to cover damages suffered by the other party not to the infringed or damaged good itself but to other legally protected interests. An exclusion of consequential loss would exclude a standstill of production, recovery for loss of use, lost profits, expenses incurred for supplementary labour, product recall as well as pure economic loss due to third party claims.

In contracts, it is advisable to define precisely which damages are covered by the term indirect or consequential damages.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

Under German law, in B2B contracts there are no special steps required for exclusion clauses to be enforceable. However, if a clause would be particularly unusual or grossly inappropriate to the other party, it could be deemed invalid.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a) Is there any requirement of reasonableness?

In German contract law, standard terms of contract including standard form contracts are of considerable practical significance. Standard terms of contract were formerly regulated under the Act on Standard Terms of Business (Gesetz zur Regelung des Rechts der Allgemeinen Geschäftsbedingungen – “AGBG”). On January 1, 2002, these statutory provisions were integrated into the German Civil Code (Bürgerliches Gesetzbuch – “BGB”).

Section 307 (and the following sections) BGB provide for regulation of standard terms by a general rule (section 307 BGB) as well as by a catalogue of prohibited terms (sections 308 and 309 BGB). The standard terms contained in the catalogue of prohibited terms are either always void (section 309 BGB)

or they are regarded as void where in an individual case it would lead to **unjustifiable discrimination against the other contracting party** (section 308 BGB). Where a term is not listed in the catalogue, it may still be void due to a violation of the general rule of section 307 BGB. Pursuant to this section, standard terms of contract are invalid **if they violate the requirement of good faith by placing an unreasonable disadvantage on the other contracting party**.

**b) Is there any ability to exclude liability for 'gross negligence'?**

The limitation of liability is enforceable, unless the loss or damage was caused intentionally or by gross negligence, which cannot be capped or otherwise limited (see section 309 subsection 7 lit. b) BGB). Moreover limiting liability is also invalid in the case of injury to life, body or health due to a negligent breach of duty (see section 309 subsection 7 lit. a) BGB).

Though a minor negligent act with regard to the material obligations cannot be effectively disclaimed, it can be limited to typical and predictable damages. Limitations can be made up to a particular amount, which must be proportional related to the risk arising out of the contract (see commentary in Palandt/Heinrichs, section 309 BGB, marginal no. 49).

**c) Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

In terms of general contract law, the contractor's obligations as to quality are contained in the BGB. In section 434 BGB, the term 'defect' is defined in detail. The wording supports the concept that the contractor has to comply with the specifications as agreed in the contract. However, if no quality obligations are agreed, the statute also requires the contractor to provide goods purchased which are fit for their purpose. German courts interpret this fitness for purpose obligation to apply in every case, even those where the expressed standards fall below the fitness for purpose standard.

**4. What happens if a limitation/exclusion fails any such legal control?**

German courts have no power to redraft an unreasonable limitation clause. The offending provision will simply be unenforceable. In most cases the remainder of the contract will remain valid with the result that the contractor has potentially unlimited liability. The same applies to exclusions from particular types of liability. Therefore, in contracts, it is advisable to draft individual exclusions as standalone, independent sub-clauses.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

In Germany, the directly affected party qualifies to be compensated for all damages incurred which can reasonably be deemed a result of a breach of contract. The strict liability of the responsible party is based on the general entitlement provided by section 280 BGB. This rule provides that the party who wilfully or negligently breaches its obligation under the contract has to pay compensation to the other party for the damages it suffered by the breach.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

German law draws a distinction between liquidated damages ('Schadenspauschale') and contractual penalties ('Vertragsstrafe'). Liquidated damages are used to assist in determining and proving actual damages, whereas a penalty clause is used to secure the performance of contractual obligations. Both types of clauses are generally permissible. Contractual penalties can be mitigated if 'disproportionate or excessively high'.



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## IRELAND

### 1. What would an exclusion of consequential loss in a contract exclude?

The position under Irish law is similar to that under English law, in that an exclusion of indirect and consequential loss does not exclude any loss which arises as a direct and natural consequence of the breach of contract. As such, by itself, it excludes relatively little.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

Not as such in a B2B context. It is essential that the terms which contain the applicable limitation/exclusion clauses are sufficiently brought to the attention of the other contracting party before the contract is formed. In assessing limitation/exclusion of liability clauses, the Irish courts will take into account the circumstances before them, such as the relative bargaining power of the parties and whether they have contracted with one another on the same/similar terms in the past (eg, course of dealing). In practice parties can be expected to bring to the other contracting party's attention any clauses which are particularly unusual or onerous. As is the case under English law, customers are under an obligation to make themselves familiar with the terms of any offer/proposal and to raise objections if necessary otherwise they may well be deemed to have agreed to them.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

There is no direct equivalent of English legislation, the Unfair Contract Terms Act 1977 ("UCTA"). However similar provisions to the 'reasonableness' test in UCTA apply in an Irish context by virtue of Sale of Goods and Supply of Services Act 1980 (the "Act"). Irish law subjects limitation and exclusion clauses to a 'reasonableness' test, ie the term must be 'fair and reasonable'. In practice this means almost all limitations and exclusions are subject to this test. The Act goes on to specify the factors that particular regard may be given to, including the relative bargaining position of the parties, whether another supplier could have provided the goods/services without the exception clause and whether the customer had actual or constructive knowledge of the term or its extent.

#### b. Is there any ability to exclude liability for 'gross negligence'?

Irish legislation does not recognise a formal distinction between negligence and gross negligence in a contractual context. One can therefore exclude or limit liability for both subject always to the test of reasonableness referred to above.

The Irish Courts have recently had occasion to consider the meaning of 'gross negligence' in a limitation of liability clause (*ICDL GCC Foundation FZ-LLC & Anor v European Computer Driving Licence Foundation [2011] IEHC 343* (High Court) and on appeal to the Supreme Court, *GCC Foundation FZ-LLC & Anor v European Computer Driving Licence Foundation [2012] IESC 55*). At first instance, the High Court held that 'gross negligence' meant "a degree of negligence where whatever duty of care may be involved has not been met by a significant margin". The Supreme Court upheld this view, and upheld a

clause which purported to provide that a limit on liability did not apply where damage was caused by a 'wilful act or gross negligence'. (On the facts of the case, the Courts found that the defendant acted with a significant degree of carelessness such as to amount to gross negligence so that the cap on liability would not apply. The damages limitation clause was therefore inapplicable and the plaintiffs were entitled to whatever damages arose from the defendant's breach of contract.)

**c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

Irish legislation (ie, the Act referred above) provides that where a seller sells goods in the course of a business there is an implied condition that the goods supplied are of 'merchantable quality'. As is the case under English law, these statutory implied conditions can be excluded provided that doing so is regarded as satisfying the 'fair and reasonable' test. Whether the exclusion of such implied obligations is regarded as reasonable will depend upon a number of factors but particularly what express warranties the supplier has given.

**4. What happens if a limitation/exclusion fails any such legal control?**

The Irish Courts have no power to redraft an unreasonable financial limitation clause. The offending provision will simply be unenforceable. In most if not all cases the remainder of the contract will remain valid with the result that the supplier/service provider has potentially unlimited liability. The same applies to exclusions from particular types of liability. Depending upon the precise way in which the clause is drafted the Courts may be prepared to use a 'blue pencil' ie strike through and ignore particular offending exclusions whilst leaving the remainder intact and enforceable. For those reasons individual exclusions are typically drafted as standalone, independent sub-clauses.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

There is no legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract. In Ireland, the provision of any indemnity is often strongly resisted because of the ease of recovery under such an agreement in comparison to warranties.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Under Irish law, penalty clauses are not enforceable. A contractual liquidated damages provision will only be enforceable if it represents a genuine and reasonable pre-estimate of the loss which is likely to flow from the breach. In other words, it must be a pre-agreed estimate of the loss. The use of the words 'penalty' or 'liquidated damages' is not conclusive and it is for the party in breach to show that the sum is a penalty. The concept of 'genuine' has not been interpreted in a reported case. However commentators suggest that it must mean a serious attempt to estimate the damage however unreasonable it might appear to others.

It is clear that if liquidated damages are penal in nature, rather than compensatory, then they could be struck down. However, so long as the sum payable in the event of non-compliance with the contract is not extravagant, having regard to the range of losses that it could reasonably be anticipated it would have to cover at the time the contract was made, it can still be a genuine pre-estimate of the loss that would be suffered and, therefore, valid.



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## ITALY

### 1. What would an exclusion of consequential loss in a contract exclude?

An exclusion of consequential loss does not limit a party's liability for losses which are an immediate and direct consequence of a breach of contract. In this reference, please note that normally, under Italian law, a party in breach of contract is liable vis-à-vis the other party for: (a) losses ('danno emergente') and (b) loss of profits ('lucro cessante') incurred by the other party (provided that the said losses and lost profits are the immediate and direct consequence of the relevant breach). In the case of breaches which are not due to wilful misconduct, liability is limited to losses which could be reasonably foreseen by the defaulting party at the time when the breached obligation arose.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

In a B2B context there are no specific requirements regarding the prominence of clauses excluding or limiting the parties' liability. However, please note that, in agreements governed by general conditions set forth by one of the contracting parties, clauses limiting the latter's liability may be deemed as vexatious clauses, and as such must be specifically approved in writing by the other party (for this purpose a second signature is required for specific approval of the relevant clause).

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

There is no specific reasonableness requirement for limitation of liability clauses, but they are nevertheless subject to certain limitations (see below).

#### b. Is there any ability to exclude liability for 'gross negligence'?

Under Italian law any clause that excludes or limits in advance a party's liability for gross negligence or wilful misconduct is null and void by provision of law. The same applies to clauses excluding or limiting a party's liability for acts entailing a violation of rules of public policy (eg rules safeguarding public health).

#### c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?

There is an implied warranty obligation pursuant to which the seller warrants to the purchaser that the goods sold are free from defects which render the goods unfit for the use to which they were destined or which appreciably diminish their value. This warranty can be specifically excluded in a contract, but such an exclusion is not enforceable if the seller was aware of the presence of certain defects and purposely concealed them from the purchaser.

Further obligations of fitness for purpose/satisfactory quality may arise if the seller represents that the goods sold have certain specific qualities or warrants their proper functioning for a certain amount.



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Breach of the above representations or warranties entitles the customer to seek the remedies provided by civil law (including termination of contract).

#### **4. What happens if a limitation/exclusion fails any such legal control?**

As a general rule if clauses limiting a party's liability (or any other type of clause) are by any reason deemed invalid in court, the relevant clauses shall be deemed as not enforceable, whilst the other parts of the contract shall remain in force (in Latin: *utile per inutile non vitiatur*). This applies provided that:

(a) it is deemed that the parties would have entered into the contract even if they had been aware of the invalidity of the relevant clauses; or

(b) the invalid clauses are automatically replaced by compulsory law provisions (if any).

From a practical standpoint, the invalidity of certain clauses will not entail the nullity of the whole contract unless it is acknowledged that the invalid clauses are deeply linked to the others, so that they are all reciprocally connected. In order to mitigate such risk it is advisable to draft liability limitation clauses so as to make them, to the maximum possible extent, independent and standalone articles of the agreement.

#### **5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

There are no specific restrictions applying to indemnities (meaning obligations to keep a party safe and harmless from certain losses) under Italian law. Although not required, these types of clauses are often sought since they simplify the process of proving the indemnified party's losses. This is because, in the absence of specific clauses providing for indemnification duties, a party is bound to prove not only that it actually suffered damages, but also the amount of the damages as well as the fact that they stem from the other party's breach of contract.

#### **6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Liquidated damages (meaning pre-agreed payments of certain amounts which become due upon the occurrence of certain breaches of contract) are valid and enforceable under Italian law. Limits to enforceability may arise, typically, in respect of the amount of the penalty: such amount may be diminished by judges (either autonomously or based on a party's request) if the relevant obligation has been partly performed or if the amount of the penalty is manifestly excessive, in comparison to the non-defaulting party's interest in the full performance of the relevant obligation.

The non-defaulting party's interest is assessed by the judge particularly taking into account the effects of the breach on the equilibrium between the parties' mutual obligations and the impact on the actual situation of the non-defaulting party.

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## MALAYSIA

### 1. What would an exclusion of consequential loss in a contract exclude?

The Malaysian Contracts Act 1950 contains no specific provision dealing with exemption clauses. The Malaysian courts have followed English common law when considering this aspect of the law.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

The Malaysian position is similar to that under English law in that a person who signs a document containing contractual terms is normally bound by them, even though he has not read them or is ignorant of their precise legal effect. For example, a person's signature is undisputed evidence of his assent to the whole contract, including exemption/limitation clauses, unless the signature was obtained by fraud or misrepresentation. However the court usually requires that the terms of the contract be adequately brought to his notice.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

The courts apply a strict interpretation of the exemption clause. The words of the exemption clause must be clear and exactly cover the liability that it seeks to exclude.

Where a clause is open to ambiguity, the courts also apply the *contra proferentem* rule, meaning they will construe forcibly the words of a written document against the party putting forward the document.

#### b. Is there any ability to exclude liability for 'gross negligence'?

An exemption clause however wide and general does not exonerate the party claiming the use of it from the burden of proving that the damage caused was not due to his negligence and misconduct. He must show that he had exercised due diligence and care.

However, the courts are less strict in construing a clause limiting liability in negligence than a clause excluding liability altogether.

#### c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?

Section 16 of the Malaysian Sale of Goods Act 1957 provides there is no implied warranty or condition as to the quality or fitness of goods except where:

(i) the buyer expressly or by implication makes known to the seller the particular purpose for which the goods are required, so as to show that the buyer relies on the seller's skills; or

(ii) where goods are bought by description from a seller who deals in goods of that description, there is an implied condition that the goods shall be of merchantable quality.

These implied terms however can be excluded by express agreement of the parties, by the course of dealing between the parties or by usage, if the usage is such as to bind both parties to the contract.

### 4. What happens if a limitation/exclusion fails any such legal control?

The position in Malaysia is similar to that under English law.

### 5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?

No. There are instances where there is an indemnity clause in contracts, typically to get around having to pay damages.



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## 6. Is there any rule against liquidated damages which constitute a penalty being enforceable?

There are no rules against liquidated damages which constitute a penalty being enforceable. Section 75 of Contracts Act 1950.

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## MEXICO

### 1. What would an exclusion of consequential loss in a contract exclude?

Under Mexican law consequential loss could be limited or predetermined as liquidated damages as a means to limit exposure. If consequential loss is not limited by an amount agreed by the parties the affected party will be entitled to claim it but will require broad evidence of the consequential loss. Article 377 of the Mexican Commercial Code provides guidelines on this topic.

Additionally there is some international guidance under the International Sales of Goods (which forms part of Mexican law as part of its ratification as part of the international treaties entered by Mexico)/United Nations Convention on Contracts for the International Sale of Goods/Section II Damages (articles 74 – 80). If the parties do not opt out in writing from the International Sales of Goods, they could apply. Normally, Mexican judges try to avoid invoking the International Sales of Goods but the parties through their lawyers could bring them up to clarify a topic that is not clear under the rest of our commercial legislation.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

The Mexican Commercial Code provides a similar approach to English law. In a B2B context the parties are bound to the exact terms they deem to be binding in the agreement 'literally' and not on what could be interpreted as to what they intended. Article 78 of the Mexican Commercial Code points this out.

The Mexican Commercial Code is based (originally) on the French Commercial Code (Napoleon Codification; as well as our Civil Code, etc.) It is part of the Latin-Roman Canonical Tradition. Therefore, the Mexican legal system is very similar on many topics to Spanish, German, French and Italian (among others who share the same roots) legislation.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

No.



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**b. Is there any ability to exclude liability for 'gross negligence'?**

No; civil and commercial legislation will refer you to the Federal Criminal Code provisions regarding 'gross negligence' matters. It cannot be excluded or limited by contract. A claim for damages and losses could be brought in addition to a criminal action for 'gross negligence'.

**c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

No.

**4. What happens if a limitation/exclusion fails any such legal control?**

The same scenario applies under Mexican law as under English law; the clause will be unenforceable; the rest of the contract will be valid, Article 78 of the Mexican Commercial Code points this out too.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Yes; either specific performance could be claimed or the payment of the indemnity but not both pursuant to article 376 of the Mexican Commercial Code and article 1971 of the Mexican Federal Civil Code. Again, on this matter the United Nations Convention on Contracts for the International Sale of Goods/Section II Damages (articles 74 – 80) would also apply if not opted out in writing in the agreement.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

No, liquidated damages are a subject to be agreed by the parties freely and the agreement should evidence that each party knew this.

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## THE NETHERLANDS

**1. What would an exclusion of consequential loss in a contract exclude?**

Dutch law does not clearly define consequential loss. In each case the court will have to interpret the meaning of an exclusion of consequential loss. Decisive is what the parties to a contract could reasonably expect from each other. An important factor – but not the only factor – is the common interpretation of contract language. There is case law which states that damage which is not the immediate consequence of a breach, such as a loss of profit, should be regarded as consequential loss.

**2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

No special steps are required.



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**3. Are there any legal controls on limitation/exclusion clauses? In particular:**

**a. Is there any requirement of reasonableness?**

Small businesses and consumers can demand – if certain conditions are met – the nullification of an exclusion of liability in general terms and conditions, unless the exclusion is justified in the given circumstances. Besides, also in a B2B context, a party cannot rely upon an exclusion of liability, if a court would deem the reliance upon the limitation/exclusion clause unacceptable in view of the principles of reasonableness and fairness.

**b. Is there any ability to exclude liability for 'gross negligence'?**

Gross negligence could be a reason for a court to decide that the reliance upon a limitation/exclusion clause is unacceptable.

**c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

Implied conditions can be excluded, but it is up to a court to decide what the parties could reasonably expect from each other in relation to the exclusion clause.

**4. What happens if a limitation/exclusion fails any such legal control?**

In such cases the offending provision is unenforceable, but the contract as such will remain valid.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

In principle, an indemnity in favour of a customer is enforceable. If the indemnity is regarded as a penalty clause, a court could mitigate the fixed damage. See question 6 below. The courts can also apply the test of reasonableness and fairness mentioned under question 3 above and on that basis decide that the customer cannot claim the indemnity or part thereof. It could do so if the actual damage caused to the customer is substantially lower or if the customer is (in part) responsible for the damage or refused to take reasonable steps to mitigate the damage.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Any clause which provides for a penalty, liquidated damages or which otherwise fixes damages to a specific amount, is regarded as a penalty clause. Such clauses are valid. However, a court can mitigate the penalty if and when the principle of reasonableness demands this. On the same basis, the court can also award damages which are higher than the liquidated damages. A court could amend the penalty if the relation between the penalty and the damage is (fully) out of proportion.

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## SWEDEN

### 1. What would an exclusion of consequential loss in a contract exclude?

Exclusion of consequential and indirect loss in a contract will generally exclude loss that is not a direct and foreseeable consequence of the breach of contract; loss resulting from reduction or loss of production or turnover, other loss resulting from the goods being unfit for use in the intended manner, loss of profit resulting from a contract with a third party not being performed or not correctly performed, and other similar loss, if such loss was difficult to foresee.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

Exemption clauses must be reasonably clear and distinct in order to be valid. The decisive factor is whether or not the adversary must be deemed to have grasped the meaning of the clause through standard interpretation. If the exemption clause is of an especially broad nature - such as an 'as is' clause - it is generally required that the clause is given particular attention to ensure that the other party understands its consequences. It is accepted that suppliers generally trade on standard terms that contain limitations and exclusions, and a reference to the standard terms is sufficient for them to form part of the contract provided that they are available to the other party and do not contain surprising or hardship clauses.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

Section 36 of the Contracts Act (1990:931) states that a contract term or condition may be modified or set aside if such term or condition is unreasonable having regard to the contents of the agreement, the circumstances prevailing at the time the agreement was entered into, subsequent circumstances, and circumstances in general. Exemption clauses are subject to this provision. However, the possibility to apply the provision in B2B situations where the parties have equal bargaining power is very limited.

#### b. Is there any ability to exclude liability for 'gross negligence'?

It is often stated in Swedish legal literature that exemption clauses are not upheld if the party in breach acted with gross negligence. This general rule has also to some extent been confirmed by the Supreme Court. However, it must be noted that there is no clear definition of the concept of gross negligence under Swedish law.

#### c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?

These implied conditions can be excluded provided that doing so is regarded as satisfying the test under Section 36 of the Contracts Act referred to above.

### 4. What happens if a limitation/exclusion fails any such legal control?

Under Section 36 of the Contracts Act, Swedish courts may either modify or set aside an unfair contract term. The remainder of the contract will generally remain valid. However, where a term is of such significance to the agreement that it would be unreasonable to demand the continued enforceability of the remainder of the agreement with its terms unchanged, the agreement may be modified in other respects, or may be set aside in its entirety (Section 36 of the Contracts Act).

### 5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?

Indemnities in respect of losses suffered by customers are quite common. Under Swedish law, the ordinary meaning of an indemnity is that the customer is entitled to certain contractually agreed damages if it can prove that a certain breach has effectively caused the customer's losses. Generally,



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the customer does not have to prove that the other party was negligent with respect to the breach of contract. Other than Section 36 of the Contracts Act, there are no specific legal restrictions on indemnities of this kind.

## **6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Parties often agree on liquidated damages (ie contract clauses for an agreed sum due upon failure of performance). There is generally no requirement that the harm caused by the breach is difficult to estimate. As long as they satisfy the test under Section 36 of the Contracts Act, liquidated damages clauses are accepted under Swedish law. Swedish court judgments setting aside a liquidated damages clause are extremely rare.

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## **UNITED ARAB EMIRATES**

*Note: Non-DIFC Law - The Dubai International Financial Centre (DIFC) is a separate financial free zone located in Dubai and has a number of its own laws which are in substance very similar to English law. The responses given below do not cover DIFC law but rather UAE laws in general which have application throughout the UAE save for the DIFC.*

### **1. What would an exclusion of consequential loss in a contract exclude?**

By itself, it could exclude relatively little. The UAE courts exercise wide discretion in their awards of damages. A party seeking compensation must prove the actual losses incurred and the UAE courts do tend to be conservative when assessing loss and require a close causal link between a breach and any subsequent loss for that loss to be recoverable.

### **2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?**

Under UAE law such steps are unlikely to be significant in the context of a B2B claim.

### **3. Are there any legal controls on limitation/exclusion clauses? In particular:**

#### **a. Is there any requirement of reasonableness?**

The UAE courts have the power to vary the terms of limitation/exclusion clauses where a party can demonstrate that the actual loss/damage incurred was in fact greater than the amount contemplated by the limitation of liability clause. Similarly, with regard to a liquidated damages clause the UAE courts may award a greater or lesser amount than the amount of liquidated damages if the party seeking such an alternative award can prove the actual loss suffered was more or less (as relevant) than the liquidated damages amount. Although there is certainly no harm in including limitation/exclusion of liability clauses, under UAE law these cannot definitively be relied upon.

Further there is no concept of reasonableness required for such clauses to be effective *per se*, rather the party seeking to avoid the effect of a limitation or exclusion clause will need to evidence the actual level of loss and rely on the UAE courts' discretion to award that loss notwithstanding any limitation/exclusion clause.

**b. Is there any ability to exclude liability for 'gross negligence'?**

It is not generally possible to exclude liability for gross negligence under UAE law.

**c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

There are UAE laws which provide for purchasers to have recourse where goods are found to be defective. These obligations can be excluded in limited circumstances, such as where goods are clearly sold on an 'as is' basis, the buyer is given an opportunity to inspect the goods prior to purchase and the seller does not take steps to conceal any defects.

**4. What happens if a limitation/exclusion fails any such legal control?**

As discussed above, under UAE law the issue is not really one of determining whether or not a limitation or exclusion clause is reasonable (and hence effective) but rather a case of whether the party seeking to avoid the effect of such a clause can prove that the actual loss suffered exceeds any limitation/exclusion and convincing the UAE court to exercise its discretion to override such a clause.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Under UAE law there is no restriction *per se*, but the courts' decision on enforceability will depend on the nature and scope of the indemnity being considered. It should also be noted that under UAE law there is no clear distinction between assessing damages on an indemnity basis compared to a breach of contract basis. It is certainly useful to include indemnities in respect of specific breaches or circumstances that may be likely to arise and, if possible, it should be stated clearly in any indemnity clause what types of losses the indemnified party would expect to be covered.

However, a general indemnity clause covering losses arising as a result of breach of contract does not really provide any additional protections or recourse under UAE law over and above a general breach of contract claim as the UAE courts will approach the question of assessing recoverable losses on the same basis in either case.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

Under UAE law the question is not one of whether a liquidated damages clause may be considered unenforceable if it is seen as amounting to a 'penalty' *per se*. Rather, the relevant issue is that, under the UAE Civil Code, the UAE courts have discretion to award an amount of damages that may either be higher or lower than any liquidated damages amount if the relevant party can prove to the court that such higher or lower amount is the actual loss suffered. Liquidated damages clauses are reasonably common under UAE law, however, and they do shift the burden of proof onto the party seeking to claim either more or less than the liquidated damages amount.



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## UNITED STATES

The following is based on California law.

### 1. What would an exclusion of consequential loss in a contract exclude?

An exclusion of indirect, special, and consequential damages is often found in business contracts, especially where the risk associated by such damages to one or both parties is not warranted given the economics of the transaction. Such a provision (which can be unilateral or mutual) usually excludes loss of profit or revenue or damages asserted by a third party against the non-breaching party that may otherwise be recovered if it is determined such damages were reasonably foreseeable or 'within the contemplation of the parties' at the time of contract formation.

### 2. Are any special steps required in terms of prominence (eg bold type/capital letters) or positioning within a contract for limitation/exclusion clauses to be enforceable?

The provision for exclusion of indirect, special, and consequential damages need not be of a particular font or be in bold, however, such provisions must be conspicuous in the contract which is usually accomplished through the use of a larger font, all caps or bold font (although there is no specific requirement regarding font size, etc). In contrast, in contracts for the sale of real estate, liquidated damages provisions must be of a certain size font and/or in bold, and must be initialled by the parties to be enforceable.

### 3. Are there any legal controls on limitation/exclusion clauses? In particular:

#### a. Is there any requirement of reasonableness?

By statute, to be enforceable, the limitation or exclusion in a contractual provision for exclusion of indirect, special, and consequential damages must not be unconscionable. Under California law, the doctrine of unconscionability has a substantive and procedural element. Both elements must be present in order for a court to refuse to enforce a contract as unconscionable. Procedural unconscionability concerns the manner in which the contract was negotiated and the circumstances of the parties at that time. The relevant factors are oppression and surprise. Substantive unconscionability focuses on the terms of the agreement and whether those terms are 'overly harsh' or 'one-sided'. To be substantively unconscionable, a contract must 'shock the conscience'.

#### b. Is there any ability to exclude liability for 'gross negligence'?

It is rare to see a provision in a contract that excludes liability for liability based upon negligence or gross negligence (meaning that a party would only be liable for its wilful misconduct). However, it is common to see a limitation of liability provision (either limiting the type of the damages recoverable, providing for liquidated damages or capping the amount of damages available) which carves out wilful misconduct and gross negligence. The difficulty is determining what constitutes gross negligence. Gross negligence is defined as the lack of any care or an extreme departure from what a reasonably careful person would do in the same situation to prevent harm to oneself or to others.



**c. Is there any ability to exclude implied obligations of fitness for purpose/satisfactory quality?**

A provision for exclusion of implied warranties of fitness for a particular purpose or for merchantability (these implied warranties are provided for by statute) is generally enforceable provided that it is reasonable. Such exclusions must be conspicuous in the contract which is usually accomplished through the use of a larger font, all caps or bold font (although there is no specific requirement regarding font size, etc).

**4. What happens if a limitation/exclusion fails any such legal control?**

If a limitation of liability provision or exclusion of liability provision fails to meet the necessary requirements for enforceability, it will not be rewritten or modified by the court. It will simply be unenforceable, and the remainder of the contract will be enforced without consideration of such provision. Compare and contrast to non-compete provisions which may be rewritten or modified so that they are reasonable.

**5. Is there any legal restriction on the enforceability of an indemnity in favour of a customer in respect of losses suffered as a result of a breach of contract? Are such indemnities typically sought and, if so, why?**

Indemnification provisions are common in business contracts and usually provide for indemnification for any and all claims arising out of, based upon or relating to a breach by the other party. The scope of the indemnification clause is often expanded to include indemnity claims arising out of other things such as intellectual property infringement (claims brought by a third party for infringement of that third party's patents, trademarks, copyrights). Indemnification provisions may also be subject to negotiated exclusions, and to limitation of liability provisions and/or liability caps. Indemnification provisions usually include attorney's fees for the party seeking indemnification. Indemnification provisions are often the subject of much negotiation and redrafting. There are no real restrictions on the enforceability of indemnification provisions.

**6. Is there any rule against liquidated damages which constitute a penalty being enforceable?**

By statute, a liquidated damages clause is valid unless a party establishes that it was unreasonable under the circumstances existing at the time the contract was made. However, this rule does not apply in cases in which another applicable statute prescribes a different standard (eg a liquidated damages provision in a real estate contract) and does not apply when the contract concerns the purchase or rental of personal property; a service used primarily for personal, family, or household purposes; or a residential lease. In those cases, a liquidated damages clause is void except when from the nature of the case, it would be impracticable or extremely difficult to fix the actual damage.

Additionally, the amount of liquidated damages stated in a contract also must represent a reasonable endeavor to estimate fair compensation for the loss sustained. If the stated amount is designed to substantially exceed the damages suffered, and its primary purpose is to serve as a threat to compel compliance through the imposition of charges bearing little or no relationship to the amount of actual loss, then the purported liquidated damages clause will be an invalid attempt to impose a penalty.

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