Exemption clauses have teeth – negotiate contracts carefully

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The Court of Appeal has recently provided guidance on the application of the *contra preferentum* rule in *(1) Persimmon Homes Limited (2) Taylor Wimpey UK Limited (3) BDW Trading Limited v Ove Arup & Partners Limited (2) Ove Arup & Partners International Limited*.

In this case, the defendant engineers failed to advise the claimants, a consortium of developers, of the existence of asbestos at a development site. The defendants sought to rely upon an exemption clause for liability in relation to asbestos. The claimants contended, amongst other things, that the *contra preferentum* rule, which would require the exemption clause to be interpreted in favour of the claimants, should apply. The Court of Appeal unanimously held that where parties have equal bargaining power, the *contra proferentum* rule now has a very limited role in interpreting exemption clauses and is more relevant to indemnity clauses.

Background

In January 2007, the claimants, Persimmon Homes, Taylor Wimpey, and BDW Trading (together the consortium) appointed the defendants, Arup, to provide consulting engineering services for its bid to develop the former docks in Barry, Wales (the site). The Consortium purchased the site for £53m in September 2007 with a view to constructing a commercial and residential development.

During the purchase negotiations, Arup agreed to provide further professional services to the Consortium in or around June 2007. The terms of this appointment were set out in a contract dated 22 September 2009 (the Agreement). Under the terms of the Agreement, Arup agreed to exercise reasonable skill and care in providing engineering services including but not limited to geotechnical and contamination investigation. The Agreement stated at clause 6.3 that:

"The Consultant's [Arup's] aggregate liability under this Agreement whether in contract, tort (including negligence) for breach of statutory duty or otherwise (other than for death or personal injury caused by the Consultant's negligence) shall be limited to £12,000,000 (twelve million pounds) with the liability for pollution or contamination limited to £5,000,000 (five million pounds) in the aggregate. Liability for any claim in relation to asbestos is excluded."

Arup provided warranties (the Deed of Warranty) to each member of the Consortium confirming that it had exercised and would

Any comments or queries?

Ben Goodier
Partner
+44 20 3060 6911
ben.goodier@rpc.co.uk

Claire McNicholl
Senior Associate
+44 20 3060 6349
claire.mcnicholl@rpc.co.uk

continue to exercise reasonable skill and care in performing its duties under the Agreement. The Deed of Warranty stated at clause 4.3 that:

"The Consultant's aggregate liability under this Deed whether in contract, tort (including negligence), for breach of statutory duty or otherwise (other than for death or personal injury caused by the Consultant's negligence) shall be limited to £5,000,000.00 (five million pounds) with the liability for pollution and contamination limited to £5,000,000.00 (five million pounds) in the aggregate. Liability for any claim in relation to asbestos is excluded."

Clause 6.3 of the Agreement and clause 4.3 of the Deed of Warranty will be collectively referred to as the "Exemption Clauses".

In 2012, the Consortium appointed Cuddy as groundworks contractor. Cuddy commenced the groundworks, including excavation, in May 2012 and detected asbestos in July 2012. Following this discovery, the Consortium alleged that the amount of asbestos detected was significantly greater than the amount of asbestos estimated by Arup. The Consortium alleged that Arup had failed to identify and advise of the asbestos at an early stage and commenced proceedings for their alleged losses.

The Proceedings

The Consortium issued proceedings in July 2014 in the Technology and Construction Court for negligence, breach of contract and breach of statutory duty to recover the following losses:

- the sum of £2m following the purchase of the Site on the basis that the Consortium would have purchased the Site for £51m rather than £53m, if properly advised of the asbestos
- additional costs incurred by the Consortium following the late discovery of the asbestos. The Consortium alleged that such costs could have been avoided if properly advised.

Arup denied liability for the Consortium's alleged losses, relying upon the Exemption Clauses.

Preliminary issue hearing

The TCC ordered a trial of preliminary issues to determine, amongst other things, the following issues:

Issue 2: Do the words "Liability for any claim in relation to asbestos is excluded" in Clause 6.3 of the [September 2009] Agreement and Clause 4.3 of the Warranties exclude liability for each and every claim asserted in the Particulars of Claim?

Issue 3: If the answer is negative, is Arup's liability to the Consortium for each and every claim asserted in the Particulars of Claim limited to £5,000,000.00:

(a) Under the Agreement?
(b) Under the Warranties?"

Justice Stuart-Smith answered "yes" to Issues 2, 3(a) and (b). Justice Stuart-Smith held that the meaning of the Exemption Clauses was clear, representing an agreed allocation of risk between the parties and the courts should give effect to that meaning.

The Court of Appeal

The Consortium issued an appeal on the following grounds:

- "Liability for pollution and contamination" in the Exemption Clauses was intended to mean liability for causing pollution and contamination and not any liability in connection with pollution and contamination
- the phrase "liability for any claim in relation to asbestos" in the Exemption Clauses should be construed in the same way. On this interpretation, Arup's liability was therefore allegedly excluded only if it had caused the asbestos
- the Consortium sought to argue that, in any event, reference to "liability for any claim in relation to asbestos" did not exclude liability for negligence, and

- the Consortium alleged that Justice Stuart-Smith had incorrectly failed to apply the *contra proferentem* rule, in accordance with the principles set out in The *Canada Steamships Lines Ltd v The King*, and that in view of the ambiguity in relation to the meaning of the Exemption Clauses, the words should be construed against Arup.

Interpretation of the Exemption Clauses

The Court of Appeal unanimously rejected the Consortium's appeal. In his judgment, Lord Justice Jackson agreed with Justice Stuart-Smith at first instance and held that the natural meaning of the words used should be applied. Lord Justice Jackson considered that the Consortium's suggestion that Arup would not be liable for causing asbestos, ie moving it from one area to another, but would be liable if it remained in the same area, was "nonsensical". The Exemption Clauses excluded any claim relating to asbestos. Arup was not therefore liable for any claims by the Consortium for alleged losses arising from asbestos at the Site.

The *contra proferentum* rule

Lord Justice Jackson also dismissed the application of the *contra proferentum* rule and held that, in commercial contracts involving parties of equal bargaining position, the rule has a very limited role, relying upon Master of the Rolls Neuberger in *K/S Victoria Street v House of Fraser (Stores Management) Limited* who stated that:

"rules" of interpretation such as contra proferentum are rarely decisive as to the meaning of any provisions of a commercial contract. The words used, commercial sense, and the documentary and factual context, are and should be, normally enough to determine the meaning of a contractual provision."

Lord Justice Jackson held that the meaning of the Exemption Clauses was clear and the contra proferentum rule did not change the decision at first instance.

Analysis of the *contra proferentum* rule

The authorities on the application of this rule are extensive. The rule was initially set out in the case of *The Canada Steamships v The King* and is summarised as follows:

- if the clause expressly excludes liability for the negligence of a party in whose favour the clause was made, then effect must be given to the exemption clause
- if the clause is silent in relation to the negligence, the court must consider whether the language used was sufficiently broad to include negligence. If not, then the clause must be interpreted against the party in whose favour it was made
- if the clause is interpreted to exclude negligence, the court must consider if damages would apply based upon grounds other than negligence which are not "so fanciful or remote".

Even applying these criteria, Lord Justice Jackson considered that the meaning of the Exemption Clauses was sufficiently wide to exclude negligence and there were no other grounds for Arup to pay damages to the Consortium.

As stated above, Lord Justice Jackson observed in his decision that the *contra proferentum* rule has a limited role and is clearly more relevant to indemnity clauses than exemption clauses stating that "it is one thing to agree that A is not liable to B for the consequences of A's negligence. It is quite another thing to agree that B must compensate A for the consequences of A's own negligence".

In the context of construction contracts, Lord Justice Jackson noted that parties will usually reach an agreement on the allocation risks and insurance to be obtained for these risks. Exemption clauses are a way of clearly setting out the agreed distribution of risks in the contract. It should not therefore be necessary to attempt to change these clauses at a later date.

Comment

Where parties to a construction contract are of equal bargaining position and have agreed an appropriate allocation of risk, it is clear that the courts will not interfere, so far as is possible, and, where interference is necessary, will endeavour to apply the natural meaning to Exemption Clauses.

As such, it is important that the parties clearly agree and understand the allocation of these risks as soon as possible. Such agreement should be reflected in the fees and the language used in the contract should fairly and accurately reflect the allocation of risk.

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17312

Tower Bridge House
St Katharine's Way
London E1W 1AA
T +44 20 3060 6000

Temple Circus
Temple Way
Bristol BS1 6LW
T +44 20 3060 6000

11/F Three Exchange Square
8 Connaught Place
Central Hong Kong
T +852 2216 7000

12 Marina Boulevard
#38-04 Marina Bay Financial Centre Tower 3
Singapore 018982
T +65 6422 3000