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LIMITATION OF LIABILITY IN LEGAL PAPERS : FENCES MAKE GOOD NEIGHBOURS.

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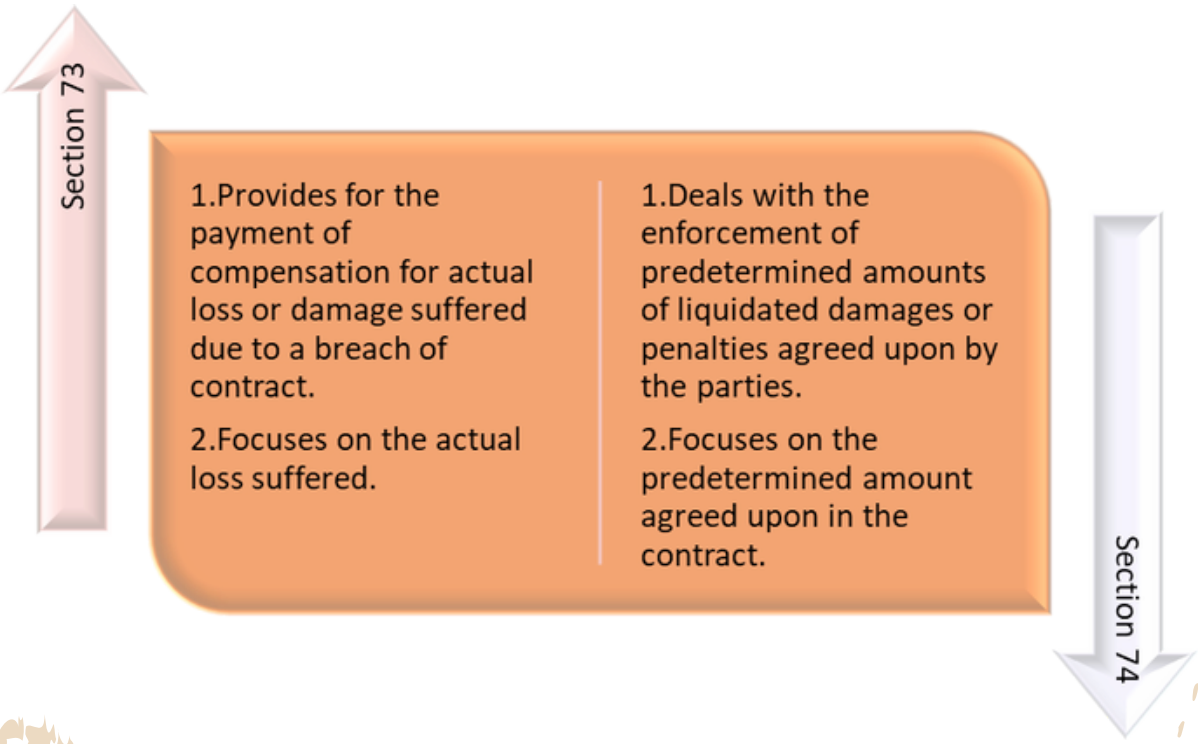
1. INTRODUCTION: [1]

A well-drafted contract is an essential part of any business or personal agreement as it helps to ensure that all parties involved can understand their responsibilities and obligations. A good written contract can help all parties involved to manage and prevent potential risk and liabilities associated with the agreement such as financial, operational, and legal risks by addressing all these risks and liabilities upfront.

Liability under a contract refers to the legal responsibility of a party to the contract for any breach or failure to perform their obligations as outlined in the contract. Under contract law, when two or more parties enter into a contractual agreement, they are bound by the terms and conditions of the contract.

If one party fails to fulfil their obligations under the contract, they may be held liable for any damages or losses suffered by the other party as a result. Damages are a common legal remedy for breach of contract.

Section 73 of Indian Contract Act, 1872 ("Contract Act") deals with the award of damages for breach of contract. It provides that the party who has suffered a loss which naturally arose in the usual course of things from such breach committed by the other Party is entitled to receive compensation. However, section 73 bars the compensation for remote and indirect loss or damages as a result of breach of contract.



[1] The article reflects the general work of the authors and the views expressed are personal. No reader should act on any statement contained herein without seeking detailed professional advice.

For calculating damages, the principle of foreseeability was laid down in landmark judgment of Hadley v. Baxendale[2]. The 'foreseeability' principle emphasises that only such losses could be compensated on breach of contract that could be reasonably foreseen by the parties at the time of contracting.

In this Article we will deal with limitation of liability clause or exclusion clause in the commercial contract which is inserted with the intention to cap the damages or limit the liability of one or more parties to the contract in case of breach or other legal action.

2. LIMITATION OF LIABILITY CLAUSE INCLUSIONS AND EXCEPTIONS

In the dynamic landscape of legal systems, the concept of limitation of liability stands as a crucial pillar, providing a protective shield for individuals and entities engaged in various professional endeavors. Parties to a contract usually insert a limitation of liability clause for certain types of losses, which may be suffered by each or either party, or to limit the amount of their liability pursuant to such loss.

The liabilities to pay damages can be limited in two ways:

a)Excluding to pay damages in certain circumstances:

To safeguard the interest of business entities from the financial liabilities in business transactions from all indirect, consequential losses adequately caused by breach of contract which are not foreseeable this limitation clause is inserted so that contracting parties absolve themselves from any indirect and uncertain nature of damages. It is a common practice for contracting parties to categorically exclude indirect and consequential damages. Even though such damages are not granted automatically in law, parties choose to make an express exclusion to avoid ambiguity.

b)Limiting the monetary liability:

The Parties to the contract cap their monetary liability of damages arising out of breach of contract. However, a well drafted contract will also have an exception to the limitation of liability clause which excludes this limitation in case breach of confidentiality clause, Indemnity clause or if there is a breach of contract as a result of negligence or fraud.

[2] Hadley v. Baxendale (1854) 9 EX 341

1.ENFORCEABILITY AND CASE LAWS ON LIMITATION OF LIABILITY

Even though enforceability of the limitation clause depends on facts and circumstances of each case, it is important that:

- Each Party has equal bargaining powers;
- Each Party has knowledge of existence of this clause in the agreement;
- Clause is clear and unambiguous;
- Clause is not unconscionable.

a. Equal bargaining powers:

For the enforceability of the limitation of liability clause it is also important that the parties to the contract have equal bargaining powers. The Supreme Court of India in **Central Inland Water Transport Corporation. v. Brojo Nath Ganguly[3]** introduced a principle that Courts will not enforce an unfair or unreasonable contract clause in a contract, entered into between parties who are not equal in bargaining power. The Court did, however, excluded applicability of this principle to cases where the bargaining power of the parties is equal or almost equal, or where both parties are businessmen, and the contract is a commercial transaction.

b. Knowledge of existence of this clause:

For enforceability of this clause, it is important that the parties to the Contract are aware of the existence of this limitation clause. In **Bharathi Knitting Company v. DHL Worldwide Express Courier Division of Airfreight Ltd[4]** the Supreme Court while dealing with a clause, which limited the liability of a courier company in case of any loss or damage to a shipment, in the terms and conditions printed on a consignment note for shipment of a package upheld the decision of the National Consumer Disputes Redressal Commission, which limited the amount awarded to the consignor for deficiency of service, to the amount specified in the limitation of liability clause. The Court held that parties who sign documents containing contractual terms are usually bound by such contract and rejected the contention that there was no consensus ad idem between the parties on limitation of liability, in view of the National Commission's finding of fact that the consignor had signed the consignment note.

[3] (1986) 3 SCC 15
[4] (1996) 4 SCC 704

C. Clear and unambiguous:

The nature of the exclusion/ limitation clauses should be expressed ex abundanti cautela[5] by using clear, explicit, specific, and unambiguous terms to allow the courts to give it a natural meaning[6]. A contractual clause ordinarily binds only parties to the contract; however, on multiple instances, the contracting parties do not actually execute the contract themselves but do so through their employees or agents. In such circumstances, the 'Himalaya clause' helps the parties to extend the benefits of the exclusion clause to such third parties working under the contract by explicitly clarifying the application of the exclusion to the employees working under the contract. The name 'Himalaya clause' originates from an English law case **Adler v. Dickson [1955]** 1 QB 158[7] concerning a ship called the Himalaya. The plaintiff in this case was travelling on a cruise ship named 'The Himalaya'. Due to the negligence of the master and the boatswain, she was injured. The ship-owner was contractually exempted from the entire liability and thus, she sued the master and the boatswain of the ship and succeeded against them for negligence and breach of duty of care. It was noted by the Court that unless the contract between the ship-owner and the plaintiff expressly or impliedly extended the effects of exclusion to the employees working under the ship-owner, which in the present case was absent, such employees cannot take benefit of the exclusion.

Under Indian law, parties to a contract may restrict liability for damages through the inclusion of express provisions in the contract stating that no compensation will be payable in specific cases or that the liability will be limited only to certain kinds of damages. The Courts invoke interpretative mechanisms when the clause is ambiguous about peculiar situations to ensure reasonableness in the contract. The Indian courts have done this in two ways: (i) by employing the rule of contra proferentem[8] through strict interpretation of the contract; and (ii) by reading down the clause in light of the main intention of the contract and intent of the parties.

b. Not to be unconscionable:

The Indian Contract Act does not contain any provision dealing with unconscionability per se. Nevertheless, the courts have traced the remedy under section 16, which defines undue influence, read with Section 19A, which makes the contract vitiated

[5] out of abundant caution; to be on the safe side https://www.latin-is-simple.com/en/vocabulary/phrase/569/
[6] Union of India v. Alok Kumar, (2010) 5 SCC 349
[7] https://www.casemine.com/judgement/uk/5a8ff87960d03e7f57ec1111
[8] This rule mandates the application of that interpretation which is in favour of the party other than the one who drafted the contract, which is generally done by construing the exclusion narrowly

by undue influence voidable at the option of the affected party, and have allowed arguments claiming that there was undue influence which resulted in the insertion of the impugned unconscionable clause.

In **S.K. Jain v. State of Haryana[9]** the Supreme Court of India has noted that if the parties wilfully enter into an unconscionable bargain, law cannot come to their rescue subsequently.

An illustration to Section 16 of Act clarifies this situation beyond doubt:
"[...] (d) A applies to a banker for a loan at a time when there is stringency in the money market. The banker declines to make the loan except at an unusually high rate of interest. A accepts the loan on these terms. This is a transaction in the ordinary course of business, and the contract is not induced by undue influence"[10].

In India, however, a universal presumption of undue influence is not statutorily permitted. Section 16 of the Act states that such a presumption only arises when one of the parties holds a real or apparent authority over the other, stands in a fiduciary relation to the other, or makes a contract with a person whose mental capacity has been affected.[11]

Therefore, the invocation of presumption of undue influence is useful only in limited cases like that of employer-employee transactions, and it fails to provide any remedy in a business or consumer transaction. An exception to this understanding is Section 23 of the Act. It states that a contract shall be void, inter alia, if the court regards its consideration or object as opposed to public policy[12].

The Indian courts have shown unusual resistance in invoking Section 23 in private business contracts by strictly focusing on the idea of freedom of contract.

4. UNDERSTANDING OF LIMITATION OF LIABILITY CLAUSE

The limitation of the liability clause plays a vital role in commercial agreements and therefore it is required to be well drafted after a good negotiation between the parties.
Usually, the party drafting the agreement has an upper hand in this regard. It incorporates limitation of liability clause in its favour to limit its exposure from the first draft itself.
Let us examine one of the limitation clauses mentioned in a leading global travel company website which says as follows:

[9] (2009) 4 SCC 357
[10] The Indian Contract Act, 1872, Section 16, Illustration (d).
[11] The Indian Contract Act, 1872, Section 16(2)
[12] The Indian Contract Act, 1872, Section 23

In no event will Company be liable to you for any special, indirect, incidental, consequential, punitive, reliance, or exemplary damages (including without limitation lost business opportunities, lost revenues, or loss of anticipated profits or any other pecuniary or non-pecuniary loss or damage of any nature whatsoever) arising out of or relating to (i) this agreement, (ii) the services, the site or any reference site, or (iii) your use or inability to use the services, the site (including any and all materials) or any reference sites. In no event will Company or any of its contractors, directors, employees, agents, third party partners, licensors or suppliers' total liability to you for all damages, liabilities, losses, and causes of action arising out of or relating to (i) this Agreement, (ii) any services provided by Company, (iii) your use or inability to use the Services or the Site (including any and all Materials) or any reference sites, or (iv) any other interactions with Company, however caused and whether arising in contract, tort including negligence, warranty or otherwise, shall not exceed the amount paid by you, if any, to Company as Convenience Fees, giving rise to the cause of action.

From the bare reading of the clause, we can understand that the clause is more in the favour of the company and covers the liability of the company to a greater extent. While reviewing this clause from customer's perspective it can be suggested that the clause should be modified to the extent that damages arising out of negligence should be excluded from liability exclusion and the monetary cap for the damages due to any breach should be in proportion to the entire charges paid for booking by the customer. As these terms are online, the customers have no option but to accept these terms to use the services of the website.

However, the enforceability of limitation of liability clauses is not absolute (particularly in cases involving gross and deliberate negligence on part of the service provider) and depends on merits of each case.

5. CONCLUSION:

The limitation of liability or exclusion clause for breach reduces the prospective costs and risks attached to a contractual transaction and fosters innovation, entrepreneurship, and economic growth by mitigating risks inherent in business transactions. While entering into a contract, the parties are always interdependent on their counterparts, and they work in an atmosphere of incomplete information. Therefore, limitation clauses function as a necessary security and risk-reduction mechanism to deal with the possibility of prospective liability. They become a strategic tool to account for the implications arising out of contractual obligations due to future uncertainties.

In general practice the party with more bargaining power incorporates this clause to exclude its liability to a greater extent. Once the contract in signed with this clause being onerous it is assumed that the party has agreed to the term and very rarely court interfere with the validity of this clause in the contract if its mutually agreed and signed. It is important that other party to the contract is aware of existence of this clause and negotiate it to balance it in favour of both the parties.

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