

EXCLUSION CLAUSES AND THE REASONABLENESS TEST - WHAT YOU NEED TO KNOW ABOUT THE LATEST COURT OF APPEAL DECISIONS

02 July 2018

Pre-contract, exclusion clauses are often the subject of extensive debate, as commercially they are a key part of assessing and moderating risks. When disputes arise during performance however, will an agreed exclusion clause actually be effective to limit or exclude liability?

We consider two new Court of Appeal decisions which serve as reminders that each dispute will turn on the particular terms of the contract and the factual context, but also provide an insight into the application of the "reasonableness" test under the Unfair Contract Terms Act 1977 (UCTA).

Where the clause is reasonable under UCTA *Goodlife Foods Ltd v Hall Fire Protection Ltd* [2018]

Background

- Goodlife has a frozen food factory. Hall Fire sells automatic fire sprinkler systems for commercial and industrial use. The two companies are comparable in size and annual turnover.
- In early 2001, Hall Fire provided a quotation for the provision of a fire detection and fire suppression system for Goodlife's multi-purpose fryer, which was used to cook food products which were then frozen and sold. Over a year later, Goodlife provided a purchase order and Hall Fire installed the fire suppression system - the value of the

contract was £7,490.

- On 25 May 2012, a fire broke out. Goodlife alleged that the fire originated at the fryer, and that Hall Fire's suppression system was defective in failing to suppress the fire.
- Goodlife contended that the fire caused property damage and business interruption losses of about £6.6 million. Goodlife was insured against property damage and business interruption and these proceedings comprise a subrogated claim by Goodlife's insurers.

The Contract

At first instance, the Court held that Hall Fire's standard terms and conditions applied to the Contract.

Key terms

The **opening paragraph** of Hall Fire's conditions:

"We draw your particular attention to the following specific conditions and assumptions on which the tender is based, unless qualified in our covering letter. Any contract would be based on our tender and these supplementary conditions sections 4 - 12 which **do not provide for the imposition of any form of damages whatsoever** and are based on English Law..." [emphasis added]

Clause 11 of the conditions:

"We exclude all liability, loss, damages or expense consequential or otherwise caused to your property, goods, persons or the like, directly or indirectly resulting from our negligence or delay or failure or malfunction of the systems or components provided by HFS for whatever reason. In the case of faulty components, we include only for the replacement, free of charge, of those defected parts [sic]. As an alternative to our basic tender, we can provide insurance to cover the above risks. Please ask for the extra cost of the provision of this cover if required."

Proceedings and appeal

Hall Fire was successful at first instance on the following preliminary issues: whether clause 11 was incorporated into the Contract and, if so, whether clause 11 was

reasonable within the meaning of UCTA. Goodlife appealed.

By way of context to the Court of Appeal decision, the following points were common ground between the parties:

- the claim for breach of contract was statute-barred;
- the claim in negligence was not statute-barred as the six year limitation period did not begin to run until the date of the fire;
- the terms of the Contract were directly relevant to the nature and scope of Hall Fire's duty of care.

Court of Appeal decision

The Court of Appeal unanimously upheld the first instance decision and dismissed the appeal. Newly appointed to the Court of Appeal, Lord Justice Coulson delivered the leading judgment.

Key elements of the decision:

1. **Correct approach for the Court of Appeal to take:**

Lord Justice Coulson referred to previous case law in terms of challenges to first instance decisions concerning exclusion clauses and reasonableness under UCTA - the appeal court should only interfere with the original decision if it was based on an erroneous principle or "plainly and obviously wrong". This approach would equally apply to the issue of incorporation.

2. **Incorporation - was Clause 11 particularly unusual or onerous? Even if it was, was it fairly and reasonably brought to Goodlife's attention?**

- In concluding that Clause 11 was **not** particularly onerous or unusual, the Court of Appeal emphasised that this issue had to be considered in the context of the contract as a whole. This was a one off low cost supply contract and it was not therefore onerous or unusual for Hall Fire to use such a clause to limit future liability.
- Additionally, in the last part of Clause 11, Hall Fire did actually offer the option of insurance to enable them to accept a wider liability ("As an alternative to our basic tender, we can provide insurance to cover the above risks.")

- It would be "commercially unrealistic" to suggest that the clause was not fairly and reasonably brought to Goodlife's attention. Amongst other factors, the limitation of liability was mentioned in the opening paragraph of Hall Fire's conditions. Lord Justice Coulson: "... the warning was cast in almost apocalyptic terms if that did not alert them to the effect of clause 11, then nothing would have done".
- Goodlife took almost a year to consider Hall Life's quotation - this was plenty of time to query the standard terms and conditions if anything was unclear or to be debated.

3. Was Clause 11 reasonable under UCTA?

Again, the Court of Appeal upheld the first instance decision that the term was reasonable under the test in UCTA. Relevant factors included:

- the broadly equal bargaining positions of the two parties
- the insurance taken out by Goodlife - this was "not a neutral factor....[it was a] **critical** factor in Hall Fire's favour"
- Clause 11 "... was an entirely reasonable allocation of risk in a contract worth £7,490"
- the alternative option presented by Hall Fire in the third part of clause 11.

Goodlife's appeal was dismissed. Clause 11 operated so as to exclude any liability Hall Fire may have to Goodlife in tort.

Where the clause is not reasonable under UCTA **(1) *First Tower Trustees Ltd* (2) *Intertrust Trustees Ltd v CDS (Superstores International) Ltd* [2018]**

In (1) *First Tower Trustees Ltd* (2) *Intertrust Trustees Ltd v CDS (Superstores International) Ltd* [2018], a differently constituted Court of Appeal also considered an clause against the reasonableness test under s11(1) of UCTA.

Background and contract

This dispute arose following a representation contained in replies to enquiries before contract - the grant of a lease by the Claimants (the Landlords) to CDS (the Tenant). At

first instance, the Judge held that there was a clear case of misrepresentation by the Landlords relating to the presence or not of asbestos.

Amongst other contentions, the Landlords sought to rely on a "non-reliance" clause in the lease, clause 5.8:

"The tenant acknowledges that this lease has not been entered into in reliance wholly or partly on any statement or representation made by or on behalf of the landlord."

Proceedings

The Judge at first instance concluded that this was an attempt to exclude liability for misrepresentation to which the Misrepresentation Act 1967 (the Act) applied, meaning that it would only be effective if the clause satisfied the "reasonableness" test in UCTA. It was held that it did **not** - this was challenged on appeal.

We focus on the part of the dispute relating to the effect of clause 5.8 for these purposes.

Court of Appeal - key issues on clause 5.8

In summary:

1. Did section 3 of the Act apply to clause 5.8 of the lease?

It was argued on behalf of the Landlords that clause 5.8 was not an exclusion clause falling within the Act, but rather a "basis clause" i.e. one which defines the basis on which the parties are contracting. If correct, this would mean (it was contended) that it would prevent liability arising in the first place, and so would not fall within the Act and would not need to satisfy the reasonableness test.

This line of argument was not successful. Lord Justice Leggatt observed:

"Even if, by giving the language of section 3 of the Act a strained interpretation, a distinction could be drawn between a contract term which would exclude liability and a term which would prevent liability from arising, there is no reason to draw such a formalistic distinction and good reason not to interpret section 3 in a way which omits the latter type of term from its scope."

Clause 5.8 was therefore subject to the UCTA reasonableness test as required by section 3 of the Act.

2. Was clause 5.8 reasonable under UCTA?

Lord Justice Lewison stated that this issue was an evaluative judgment for the trial judge and (reflecting the approach in *Goodlife* mentioned above) that an appeal court should be slow to interfere - here, there was no ground for interfering.

In considering the clause against the reasonableness test in UCTA, he emphasised that if clause 5.8 was effective in so excluding liability, replies to enquiries before contract would become worthless.

Again, in this case also, the Court of Appeal unanimously upheld the first instance decision. Clause 5.8 was therefore ineffective in this claim and the Landlords were liable for misrepresentation.

Commentary

In these two Court of Appeal decisions handed down one day apart, one exclusion clause was upheld and one was ruled ineffective, both judged against the reasonableness test in UCTA.

Rather than indicating conflicting approaches by the courts however, the two decisions remind us that each clause (as Lord Justice Coulson put it in *Goodlife*) "... has to be considered in both its contractual and factual context. Some clauses will fall one side of the line; some the other. It is impossible to lay down prescriptive rules...".

Interestingly, Lord Justice Coulson did then go on in *Goodlife* explicitly to align himself with what he described as "...the trend in the UCTA cases decided in recent yearstowards upholding terms freely agreed.....".

This may be the case, but in these two judgments under review, the differing decisions flowed directly from the contract wording and (as above) the factual context. There are clear distinctions which support the approach in each, rather than suggesting a conflict in the analysis applied. In *Goodlife*, Lord Justice Coulson reflected as follows: "UCTA remains in force to protect against unconscionable behaviour, I consider that it still has a

valuable role to play. But I am in no doubt that there was no unconscionable behaviour on the part of Hall Fire, so in this case there is nothing for UCTA to protect against" - clearly confirming a case by case approach.

Whilst it is not therefore possible to lay down prescriptive rules in terms of UCTA reasonableness, there are some common themes that can be taken into account in order to protect your position as far as possible.

In our [recent article on limiting and excluding liability](#), we set out points to consider when negotiating limitation or exclusion of liability clauses. The recent Court of Appeal decisions do not substantively change the position but highlight again that these clauses need to be considered in the context of the whole contract between the parties. The courts remain reluctant to interfere with commercial contracts but it does happen - each case will be determined on its own facts but you can best protect your business by being aware of the risks and/or uncertainties that can arise from exclusion and limitation clauses.

If you have any queries on this or any issue, please contact Ashley Pigott or Andrew Smith.

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Author(s)

Ashley Pigott

Partner - [Birmingham](#)

 Email

ashley.pigott@gowlingwlg.com

 Phone


+44 (0)121 393 0543

 vCard

Ashley Pigott

Andrew Smith

Partner - Birmingham

 Email

andrew.smith@gowlingwlg.com

 Phone

+44 (0)370 733 0643

 vCard

Andrew Smith

Cathy Moore

PSL Principal Associate - Birmingham

 Email

cathy.moore@gowlingwlg.com

 Phone

+44 (0)121 393 0888

 vCard

Cathy Moore