

## 2000 Newsletter Articles

### Summer 2000

#### E-MAIL AND THE LAW

*By Marc H. Supcoff, Esq.*

The exploding use of e-mail has dramatically changed the way clients do business and the manner in which they communicate internally and externally. This article will briefly examine important issues surrounding the use of e-mail by clients in their business relationships, including the legal implications of e-mail for pre-trial discovery and litigation purposes.

E-mail is an easy and fast way for clients to communicate and to transmit and receive documents. A computer with access to the Internet or other e-mail access is all that is necessary. With the click of a mouse, an individual can send electronically and practically instantaneously a message or document to a colleague in the office, a vendor across town or a client across the country. This quickness and convenience often results in communications by clients that are considerably more informal than a letter carefully drafted, edited and revised multiple times before being sent. An English professor and writer whom I heard speak several years ago noted that e-mail had changed for the better the way his students thought about writing. Instead of talking on the telephone or procrastinating before writing and sending a letter, his students were using e-mail regularly and thus writing more often. While there is little doubt that the advent of e-mail has significantly increased the amount of written communications, e-mails present a host of thorny legal issues that perhaps the English teacher never contemplated.

One problem is that unless the e-mail drafter takes time to revise, edit and proofread the e-mail message before sending it, it may contain typographical and other errors which would not normally be found in a carefully written and edited letter. Innocent mistakes can have profound impact when contained in a letter or agreement transmitted by an e-mail message.

#### Internal E-Mail

The widespread usage of internal e-mail by employees presents a number of issues which firms need to carefully consider. Internal email may be discoverable during litigation, as discussed below. In addition, many employees are able to forward a message to user groups or private mail lists, either within the firm, outside the firm, or both. This raises the possibility that a confidential message, perhaps containing proprietary information, can be sent, inadvertently to everyone in the firm as well as to outsiders. In addition, firms need to monitor the use of internal e-mail by employees to make sure that internal e-mail do not contain inappropriate language or offensive graphics which might violate firm policies concerning sexual harassment or workplace anti-discrimination laws.

### **Keeping E-mail Confidential**

A host of confidentiality issues arise in connection with the use of e-mails. For example, who is entitled to receive an e-mail message or document? Who actually has access to the e-mail message or document? When the message is deleted from the sender and/or the recipient's e-mail folder does it still exist somewhere else? For how long? In office computer systems, firms often create back-up files to copy documents each night or at a regular interval to insure against inadvertent corruption of a document file or computer system failure. Should such back-up systems routinely include copying e-mail messages? If so, who should have access to the back-up e-mails and for how long before the messages are destroyed? Should a firm have the right or obligation to review the number and/or content of e-mail messages sent by employees? If an e-mail is not successfully transmitted to the intended recipient, should anyone other than the sender be included in the routing of the return of the message?

### **Dealing With Actual Or Anticipated Litigation**

These questions become even more critically important to individuals and firms involved in or who may be involved in litigation in the future. One suggestion is to treat e-mails no differently than a document sent by facsimile. Thus, similar to the warning contained on many fax cover sheets, and on almost all faxes sent and received by lawyers, an e-mail user may choose to include a caveat at the bottom of the message advising that the information contained in the e-mail message and/or attachment is intended only for the personal and confidential use of the designated recipient. The warning should also indicate that the message may be a privileged and confidential attorney-client communication and, that if the reader is not the intended recipient, the e-mail has been received in error and should not be disseminated or copied, and the e-mail should be deleted immediately and the sender notified by telephone.

### **Discovery of E-mails**

As a general rule, computerized data is discoverable. Thus, even if a party produces a hard copy of electronic evidence, he or she may still be required to produce the electronic version.

Counsel may request discovery of electronic mail during discovery. However, opposing counsel may challenge such discovery resulting in higher litigation costs and delays. Early in the litigation process, counsel may put the other side on notice that it is looking for specific categories of information, including the types of information sought and the specific persons whose computers may be examined.

Requests for discovery of e-mail messages, whether in an employee's inbox or outbox, deleted file or the firm's back-up file, must be made timely since many companies keep back-up files for a relatively short period of time only. A company may purposely decide to retain e-mail messages on a back-up file for a shorter period of time to avoid problems connected with electronic discovery.

### **Developing A Document Retention Policy For E-mail**

This practice may be acceptable as part of a well thought out corporate document retention policy. However, as a general rule, once a company is engaged in litigation or anticipates litigation on a particular issue in the future, it is not proper to

deliberately dispose of e-mail messages or e-mail documents which may be needed and required by a party in the litigation.

### **Conclusion**

Clients need to think carefully about how their employees use e-mail to conduct business and for other purposes. While e-mail offers the ability to communicate and do business efficiently and economically, it also creates an electronic paper trail which can be obtained by intended - and unintended- recipients. E-mail also may be required to be produced during the discovery phase of a lawsuit. While encouraging the use of e-mail by employees for legitimate business purposes, where appropriate, firms need to take necessary steps to make sure that the usage of e-mail is not abused, and that adequate safeguards are incorporated into a firm's overall document creation, storage, and retention systems.

## **CRITICAL ANALYSIS OF THE NEW AIA-B141-1997 EDITION (PART III)**

By: Michael K. De Chiara, Esq.

This is Part III of a multi-part series of articles critically analyzing the new 1997 edition of the American Institute of Architects Standard Form of Agreement between Owner and Architect with Standard Form of Architects' services, AIA, B141-1997 ("B141-1997").

This article is somewhat unique because it will focus on one new sentence in the B141-1997 form of agreement. New Section 2.1.7.1 is, for the most part, a restatement of old Subparagraphs 2.25, 2.3.2 and 2.4.3 with one critical difference. The prior Subparagraph 2.2.5, obligated the Architect to provide the Owner with a preliminary estimate of construction costs at the end of the Schematic Design Phase. Prior Subparagraphs 2.3.2 and 2.4.3 obligated the Architect to provide the Owner with adjustments to its preliminary estimate of construction costs at the end of the Design Development and Construction Document Phases, respectively. However, the last sentence of the new Section 2.1.7.1 now states: "If at any time the Architect's estimate of the Costs of Work exceeds the Owner's budget, the Architect shall make appropriate recommendations to the Owner to adjust the Project's size, quality or budget, and the Owner shall cooperate with the Architect in making such adjustments." This sentence fundamentally changes the role of the Architect regarding responsibility for controlling construction costs.

Previously, the Architect merely advised the Owner of adjustments or changes in its preliminary estimate as the project progressed. If the costs of the Project grew, the Owner had several options. However, the Architect was not responsible for making recommendations to bridge the gap between estimated costs and the Owner's budget. More importantly, the Architect would be compensated for preparing changes to meet the Owner's budget not caused by his own failure to follow the Project program.

Under the new B141-1997 form of agreement, the Architect now takes on a much more proactive role in controlling that the Architect's preliminary cost estimate match the Owner's budget through the completion of the Construction Documents Phase. In effect, the Architect is now contractually obligated to provide recommendations to Owner which will bring the estimated cost of the Project into line with the Owner's budget through the Construction Document Phase as part of the Architect's basic services. The most problematic phrase in this new and troubling sentence is set forth in the last twelve words which state, "and the Owner shall cooperate with the Architect in making such adjustments." The problems presented by this phrase are several: (1) there are no boundaries for the "adjustments" necessary to bring the Architect's estimate of cost into line with the Owner's budget that is to say, this is a totally open-ended obligation; (2) as a result of (1), the amount of design work necessary to adjust the Architect's estimate is unbounded and thus totally open-ended notwithstanding the potential mismatch of the Owner's evolving program with the Owner's budgetary constraints which should not be cost absorbed by the Architect; and (3) the Architect is bound to provide redesign services for free notwithstanding the fact that he or she might not have done anything improper but due to factors unrelated to the Architect's services which may have affected the cost of the Project.

Thus, this one new sentence appears to be a representation that the Architect will now make all modifications necessary to its documents as may be necessary to bring them into conformance with the Owner's budget through the completion of Construction Documents. The results of this sentence could be catastrophic for any Architect retained on a large complex project, as well as for smaller architects working on more modest projects. Providing redesign work, essentially for free, is a quick path to financial ruin. Why this sentence now appears in a standard AIA document is at best perplexing. This major problem is amplified significantly when the Architect is also retaining the consultants on a project and all their services are also provided for free or, in the worst case, the unwitting Architect has to pass this unreasonable burden onto his or her consultants and ends up in the preposterous and catastrophic situation of not only performing substantial work for free, but being obligated to pay the consultants for the same work it is already losing money on. Unfortunately, stranger things have happened to Architects with some regularity.

What is also very troubling about the new sentence at the end of new Section 2.1.7.1 is that it assumes that the primary reason that the Owner's budget has been exceeded is due to the work of the Architect. On large sophisticated projects especially, this is often not the case. Project cost escalations can be driven by any number of external factors (e.g. poor estimating by the general contractor or construction manager, and escalation in the cost of labor or materials, to name but two of many). In addition, the Owner's budget and its underlying assumptions may be incorrect or unreasonable. However, in the past, if that was the case, the Architect's additional work in revising its plans and specifications and those of the consultants would be borne by the Owner unless it was solely the Architect's or the consultant's professional negligence

which caused the Owner's budget to be exceeded. In addition, the Architect may now be responsible for the risk of the escalation in the cost of labor and materials from the inception of its services through the completion of the Construction Documents Phase. How does this serve the interests of the Architectural community?

In the interest of thoroughness, it should be noted that Section 1.3.3. "Change in Services" gives the Architect an argument that it should be compensated by the Owner for the redesign to bring its cost estimates in line with the Owner's budget through the Construction Documents Phase. However, this argument is not strong for several reasons. If the Architect "recommends changes" to be initiated to meet the Owner's budgetary requirements, this does not neatly fit into a "Change in Service" as defined in B141-1997. Next, Section 2.1.7.1 contains no cross-reference to Section 1.3.3, and the legal construction of the new contract to read Section 2.1.7.1 to include Section 1.3.3 is, in my opinion, a weak argument. At best, the Architect is left with a difficult legal and factual debate which by its nature generally favors the Owner.

Thus, the simple inclusion of the new sentence at the end of the new Section 2.1.7.1 will have ramifications which may well impose catastrophic obligations on Architects working on large projects. Was this the intended effect of this language? Of course not. Will it be the actual effect? Perhaps. And that is a frightening thought.

### **Nice Guys Finish In Court**

By Robert L. Honig

The telephone rings at our local architect's office. The worried voice of the owner of a construction project for which our architect completed his design services over five years ago states hurriedly "We have some problems over at the mid-town project." Puzzled, the architect asks: "Didn't we finish that project nearly four years ago?" "Yes," responds the owner, "but we've had some problems maintaining the curtain wall and I thought you could provide some assistance." Already swamped with current work, but eager to work for this prestigious owner at some time in the future, the architect, realizing that he will not be paid for his efforts, meekly states that he will meet the owner at the site tomorrow.

Most design professionals have received this phone call at one time or another, but few recognize its inherent dangers. In an effort to either nurture an existing relationship or simply assist a trouble-plagued owner or contractor, architects and design professionals often agree to return to the site of a construction project many years after the completion of their design services to help solve some sort of construction or maintenance problem without receiving any compensation. Such "return performances" typically result in the design professional, after one or more visits to the old site, offering some rather simple design recommendation to help alleviate the problem. While the good-samaritan efforts of the design professional no doubt please the owner who takes

full advantage of this free advice, the decision to “lend a hand without receiving any compensation” is fraught with trouble for the architect or engineer.

The primary problem with providing free additional advice or services *after* the performance of one’s design contract is that it tends to give the appearance that the design professional did something wrong initially. While this problem also presents itself when a designer agrees to work for free without having had performed any prior work, it is even more dangerous when the design professional has already provided some services. Either way, the design professional typically provides these free services without a written agreement. Consequently, the design professional obtains no benefit from its work and often buys itself a potential lawsuit, not only for the new services it provided, but for its original design services as well. Without a written agreement, the designer has no means of proving the limited scope of the free service he has agreed to provide. This leaves the design professional susceptible to all types of claims for work that it never agreed to perform.

Oftentimes, an owner seeks the design professional’s advice in connection with a problem that is really construction or, even more frequently, maintenance related. If the owner’s maintenance program is not improved after the design professional offers its subsequent services, the problem will likely resurface and continue. As the problem worsens and the owner spends more and more money to solve the problem, he will no doubt reach a point where he seeks to recoup his losses from any vulnerable party he can find. As the owner retraces the history of his problem, he recalls that meeting where the design professional provided some additional service several years earlier. The owner then meets with his lawyer, who instantly concocts a complaint

for professional negligence against the design professional for both the subsequent “good samaritan advice” *and the initial design services*. When the design professional incredulously questions the owner about how he could sue him when he agreed to work for free as a favor, the ungrateful owner counters that the design professional’s relationship with the owner never terminated and that the design professional’s agreement to provide subsequent advice constitutes an admission that its initial design services were performed negligently. Thus, the design professional who agreed to provide additional services merely as an accommodation to an owner or contractor in an effort to foster good will or assist a former client now finds itself in the unenviable position of defending a lawsuit involving work for which it received no compensation and which was performed so long ago that the design professional no longer possesses the documentary records needed to prepare a defense. So much for being a team player.

Naturally, the best solution for any design professional in this position is to negotiate some sort of fee, even a minimal one, for any additional services. The foregoing scenario can also be avoided, however, by preparing a simple written agreement for any and all free services performed by a design professional. The agreement should clearly state that the new services are being performed pursuant to a new contract and that the prior contract, if one existed, had been completely performed however many years earlier. A simple one-page agreement can also clearly define the limited scope of the free services to be provided by the design professional.

If no fee can be negotiated, the new agreement can confirm that the design professional is not being paid for its fee for the new services, but it should then also contain a statement that the design professional’s agreement to work for free is not an admission of any type of negligence in connection with its prior design services. If an owner is unwilling to execute such an agreement, it may be better for even the struggling design professional to politely refuse to return to the site of a troubled project, especially since the alternative leaves the design professional susceptible to a claim that it only agreed to work for free because it recognized its own prior negligence in its initial services. This simple agreement should help to diffuse the perception amongst certain owners and contractors that the design professional, particularly the architect of record, serves as the insurer for an entire construction project for its entire life. The three-year statute of limitations was enacted to protect design professionals by establishing a realistic deadline for the assertion of claims and the design professional community should not cede this protection through its efforts to please ungrateful owners or contractors.

## **BUILDING A SAFE HAVEN: LIMITATION OF LIABILITY CLAUSES**

*By Francine M. Chillemi, Esq.*

Lawyers representing engineers, architects, and contractors certainly cannot prevent problems from arising at construction sites, nor can they prevent claims from

being made against their clients. What they can and should do, however, is attempt to minimize the exposure of their clients by drafting and negotiating appropriate protections in construction-related agreements. A limitation of liability clause, in particular, may act as an effective safety net when legally enforceable.

Contractual limitations of liability have received approval from professional engineering societies as an “acceptable response to the liability crisis that threatens the profession.” Limitation of liability clauses have increasingly become “a fact of everyday business and commercial life” as a method of allocating unknown or indeterminate risk. Design professionals have been encouraged to consider limitation of liability provisions in the following circumstances:

- (1) Where liability exposure arises out of circumstances which are unique or new, or about which there is limited experience;
- (2) Where liability risks are disproportionately high in comparison to the fee to be earned from the project;
- (3) Where insurance to cover the risk is not available or available only at unreasonably high cost, or
- (4) Where a judgment in excess of a certain amount would have a severe adverse impact on the financial viability of the engineer’s business.

The most common types of liability restrictions are based on (1) available insurance coverage; (2) a specified dollar amount, “price,” “sum,” or “fee”; or (3) re-performance of the services at issue.

### **Judicial and Legislative Treatment**

Regardless of how carefully drafted it may be, a limitation of liability provision is worthless if unenforceable. Legislatures and courts throughout the country have expressed divergent opinions when deciding on the enforceability of limitations of liability clauses favoring parties engaged in design or construction activities. Accordingly, the prospective drafter of a limitation of liability clause must become familiar with legislative and judicial treatment received in the state in which the contract is being made or enforced.

Several states have specifically endorsed limitation of liability clauses in certain situations, while others have registered disapproval. Statutes often provide a foundation for courts to either approve or reject contractual provisions limiting liability. In states that have not enacted specific legislation governing limitations of liability clauses, courts have looked to anti-indemnity statutes by analogy and have relied upon public policy and general principles of contract construction. California, Illinois, Indiana, Louisiana, Massachusetts, North Carolina, New Jersey, New York, Pennsylvania, and Texas have specifically endorsed limitation of liability clauses through varying approaches. Alaska, Oregon, Virginia, and Wisconsin have created an unfavorable climate for limitation of liability clauses.

## **Factors Influencing Enforceability**

While it is difficult to formulate a precise rule for the approach that will be taken by courts ruling on limitation of liability clauses in states which are not bound by statutory or judicial precedent, courts may consider the factors set forth below.

### □ General Rules of Contract Construction

Since the enforceability of contract language frequently turns on principles of contract construction, drafters of construction-related agreements should be cognizant of these general rules. For example, public policy generally favors the freedom of parties to freely negotiate and enter into contracts. Courts must read contracts as a whole, and they must interpret them in such a manner as to give effect to every provision. Normally courts will enforce an unambiguous contract as written and will not make a better contract for either of the parties. However, it must be remembered that limitations of liability clauses will be strictly construed against the party seeking to rely upon them. The parties' expectations may be considered by the court in evaluating the meaning and enforceability of a contract. The New Jersey Superior Court in Marbro, Inc. v. Borough of Tinton Falls, for example, determined that the party seeking to rely upon the limitation of liability clause at issue was justified in the assumption that the other party to the contract would honor the provision.

### □ Type of Damages at Issue

Whether the damages sought against a design professional are based on contract or tort theories may be determinative in the court's decision with regard to enforceability. Contract law has been found to be particularly well-suited to commercial controversies because the supplier of materials or services can restrict its liability, within limits, as a factor in determining its contract price. Given that commercial contracts generally do not involve large disparities in bargaining power, courts have avoided intruding on the parties' right to allocate risks through contracting.

### □ Reasonableness of the Liability Cap

In determining the enforceability of limitations of liability, some courts have made a comparison between the total contract price, the value of the work to be performed by the party seeking to limit liability, the nature and amount of the liability limit, and the potential damages resulting from that parties' future acts, omissions, or breach of contract.

The test employed by one Pennsylvania court was whether the liability cap is so minimal compared with the expected compensation that a party's concern about the consequences of its own breach is "drastically minimized." The developer in that case sought \$2,000,000<sup>+</sup> in damages while the liability cap (\$50,000) was already approximately seven times the architect's fee. The court found this limitation to be a reasonable allocation of risk between two sophisticated parties such that it did not violate public policy against immunizing parties from liability. Significantly, the clause at issue also provided that, if the developer found the terms of the agreement unacceptable, "an equitable surcharge to absorb the Architect's increase in insurance premiums will be negotiated."

Another court applying Pennsylvania law commented that the limitation of liability clause under examination, which did not offer a choice of a reduced contract price for the limitation of

liability, “purportedly limits...liability to zero, and thus seemingly removes [the]... incentive to perform with due care.” Even so, the court did not immediately invalidate the clause. Instead, it simply denied a motion to dismiss on the ground that the court was unable to determine in that context “whether the purported limitation is reasonable.” The court apparently intended to proceed with a balancing test to determine whether the subject limitation of liability met prevailing notions of fairness. Other courts have explicitly stated that it is improper for a court to make a determination as to what is a fair and reasonable limitation of liability when the parties have already negotiated and accepted certain contract terms.

□ Clarity of the Instrument

“[W]hen all is going well and work is performed as required, no one cares too much about the nomenclature of the parties. But, when disaster strikes, precision becomes paramount.” The clarity of language in the instrument seeking to limit liability will often be considered by the court making a determination of enforceability.

□ Sophistication and Bargaining Power of the Parties

Agreements to exonerate a party from liability or to limit the extent of the party’s liability for tortious conduct [or breach of contract] are not favorites of the courts but neither are they automatically voided. The treatment courts accord such agreements depends upon the subject and terms of the agreement and the relationship of the parties.

In deciding whether to enforce a limitation of liability clause, the courts have considered the relative sophistication of parties, whether they have been represented by legal counsel, whether they are individuals or corporations, whether they have specialized knowledge of the subject matter of the contract, whether the transaction is at “arm’s length,” and whether the clause was negotiated or, at least, whether the parties had the opportunity to negotiate. negotiated or, at least, whether the parties had the opportunity to negotiate.

□ The Doctrine of Unconscionability

The doctrine of unconscionability is most often cited in connection with analysis of contracts governed by the Uniform Commercial Code. Although there is no single definition of “unconscionability,” the United States Supreme Court has described an “unconscionable” contract as one “such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other. An imbalance in terms or bargaining power will not automatically render a contract unenforceable unless the unfairness reaches “an extreme or alarming level....[T]he challenged bargain must be distinctly beyond the permissible range of advantage allowed to one of the parties so that the bargain shocks the conscience of the court.”

The Restatement (Second) of Contracts notes that contracts may be unconscionable when they are the result of deception, compulsion, unequal bargaining power, and when the weaker party had “no meaningful choice” or did not actually assent to the contract terms.

However, the court in Amoco Oil Co. v. Ashcraft, warned against the danger of courts trying to protect parties in a weaker bargaining position:

The problem with unconscionability as a legal doctrine comes in making sense out of “meaningful choice” in a situation where the promisor was not deceived or compelled and really did agree to the provision that he contends was unconscionable. Suppose that for reasons unrelated to any conduct by the promisee the promisor has very restricted opportunities. maybe he is so poor that he can be induced to sell the clothes off his back for a pittance, or is such a poor credit risk that he can be made (in the absence of usury laws) to pay an extraordinarily high interest rate to borrow money that he wants desperately. Does he have a “meaningful choice” in such circumstances? If not he may actually be made worse off by a rule of nonenforcement of hard bargains; for, knowing that a contract with him will not be enforced, merchants may be unwilling to buy his clothes or lend him money. Since the law of contracts cannot compel the making of contracts on terms favorable to one party, but can only refuse to enforce contracts with unfavorable terms, it is not an institution well-designed to rectify the inequalities in wealth.

One court has observed that it is rare to find an unconscionable limitation on consequential damages in a contract between “experienced businessmen” in a commercial setting.

□ Subjective Public Policy Considerations and the Tunkl Test

The court in Viner v. Brockway recited six highly subjective factors to be reviewed by courts deciding whether an exculpatory contract is void as contrary to the public interest. These factors were outlined in Tunkl v. Regents of the University of California:

- (1) The contract concerns a business of a type generally thought suitable for public regulation;
- (2) The party seeking exculpation is engaged in performing a service of great importance to the public, which is often a matter of practical necessity for some members of the public;
- (3) The party holds himself out as willing to perform this service for any member of the public who seeks it, or at least for any member coming within certain established standards;
- (4) As a result of the essential nature of the service, in the economic setting of the transaction, the party invoking exculpation possesses a decisive advantage of bargaining strength against any member of the public who seeks his services;

- (5) In exercising a superior bargaining power the party confronts the public with a standardized adhesion contract of exculpation, and makes no provision whereby a purchaser may pay additional reasonable fees and obtain protection against negligence;
- (6) Finally, as a result of the transaction, the person or property of the purchaser is placed under control of the seller, subject to the risk of carelessness by the seller or his agents.

The Viner case involved a failed gabion blanket system intended to remedy a landslide condition at the Los Angeles residences of plaintiffs Viner and Cousins. Defendants McCutchan and Leighton were retained by plaintiffs' attorneys to provide civil/soils engineering services and project management for the planning, design, and construction of a remedial repair of the unstable slope condition. The Viner appellate court noted that the trial record was "replete with substantial, relevant evidence, which when subjected to the test of the characteristics enumerated in Tunkl...sustains the trial court ruling that the liability limitation clauses are unenforceable." Among the evidence considered was the lack of technical qualifications of plaintiffs and their attorneys, and their disparity in bargaining position as compared with Leighton and McCutchan.

Giving short shrift to the "compelling arguments of appellants and amici regarding commercial stability and certainty as well as the economic ramifications for engineering professionals....," the Viner court directed these issues to be raised with California's legislature, not its courts. The court concluded, "In the meantime, issues of public policy and (un)conscionability are alive, well and operative within the context of Civil Code § 2782.5 and liability limitation clauses."

The Viner decision represents the furthest reach of the California courts in trampling on the rights of design professionals and other parties to construction-related contracts to negotiate freely and allocate risk. It suggests that some courts, when faced with an emotional or high-profile case, can rationalize almost any decision under the guise of "public policy." In addition, the Viner court's reasoning appears flawed in confusing the concepts of exculpatory clauses and limitations of liability.

#### □ Intentional Acts and Gross Negligence

Most, if not all, of the jurisdictions which have ruled on the propriety of limitations of liability clauses are in agreement that limitations of liability will not be enforced if the party seeking the limitation has committed an intentional, grossly negligent, or fraudulent act in connection with the contract. In L.Luria & Son, Inc. v. Honeywell, Inc., defendant Honeywell was found to have made a false promise in order to induce plaintiff to enter into a contract. The court upheld the exculpatory clause and limitation of liability clause on the breach of contract and breach of warranty claims against Honeywell, but refused to extend the protection of such clauses to the intentional tort (fraud) counts in the complaint. "Fraud is an intentional tort and thus not subject to

the cathartic effect of the exculpatory clauses found in contracts such as the one in the present case.”

In general, if the conduct of a party “smacks of intentional wrongdoing” or “betokens a reckless indifference to the rights of others,” a limitation of liability clause is unlikely to be upheld.

### **Considerations**

In order to increase the likelihood of having a limitation of liability provision enforced, drafters of such provisions should consider the following:

- (1) Be cognizant of the judicial and legislative climate in the states in which the clause may be enforced. Pay particular attention to (a) statutes prohibiting or endorsing indemnification agreements, exculpatory clauses, and limitation of liability clauses; (b) rules and laws governing architects, engineers, and others in the construction industry; and (c) general rules of contract interpretation as determined by the appropriate jurisdiction(s);
- (2) In appropriate situations, include a choice of law provision that will allow interpretation of the contract by courts of a state which recognizes and favors limitation of liability provisions;
- (3) Draft the limitation of liability clause to be as “clear and unambiguous” as possible, setting forth in plain view in the contract explicit language regarding the risks and parties to be covered;
- (4) Include an option for the party against whom the provision will be enforced to increase the contract price in return for an increased liability cap, or no cap at all;
- (5) Discuss the clause with the owner or other parties against which it is likely to be enforced prior to execution of the contract;
- (6) To avoid invalidation of the clause on the basis of “unequal bargaining power,” ensure that all parties to the contract are represented by competent counsel and that they understand the limitation of liability clause, as well as all technical issues related to the contract that may form a basis for potential liability;
- (7) Ensure that the clause covers both contract and tort damages, as well as intentional acts, in the event that the pertinent jurisdictions do not invalidate limitation of liability clauses in such circumstances and;
- (8) Use limitation of liability clauses setting forth liability caps of \$50,000 or less to defeat federal diversity jurisdiction when advantageous.

**Conclusion:**

Limitation of liability clauses, when enforced, can lessen the financial sting a lawsuit alleging tort or contract claims involving construction-related services. Drafters of these contractual provisions should become familiar with the current state of the law in the pertinent jurisdiction, with particular emphasis on any statutes which may be in effect. Given the changing landscape of the law and construction industry, however, creativity is called for in drafting and negotiating provisions limiting liability. Design and construction firms may find themselves conducting business in more than one state and, therefore, their contractual relationships may be subject to scrutiny by courts outside their domicile. Ultimately, practitioners need to be sensitive to the controlling judicial and legislative perspectives regarding limitation of liability clauses, and then appropriately tailor each clause in response to the facts presented.