Enforceability of Net Contribution Clauses

The Court of Appeal’s recent decision in the case of West v Ian Finlay Associates, published on 27 March 2014, provides welcome guidance on the enforceability of net contribution clauses. This is an area in which we have seen few reported decisions and the case provides several useful reminders for parties seeking to rely on such clauses.

The original decision from the Technology & Construction Court in the case of West v Ian Finlay & Associates (a firm) [2013] EWHC 868 (TCC) held that a net contribution clause in the architect’s appointment was unenforceable. In particular, the clause was found to be unclear and, pursuant to the Unfair Terms in Consumer Contracts Regulations 1999 (“UTCCR”), should be interpreted in favour of the consumer, the client in that case.

The Court of Appeal has now looked at the issue and their Judgment provides some useful guidance on the enforceability of such clauses.

Net contribution clauses

As explained in our update on the original decision, net contribution clauses are typically relied on by parties in the construction industry to limit the extent of their liability in circumstances where other parties may also be responsible for the same loss. This is necessary because, where two or more parties are liable for the same damage, they are jointly and severally liable for the whole of the loss and any party could be pursued for the whole of the damage.

Although The Civil Liability (Contribution) Act 1978 provides some protection in these circumstances, allowing a fair and equitable contribution to be recovered from other parties who were also responsible, there are several disadvantages. There will be some cost to the original party to pursuing such an action, as well as a risk that the other parties may become insolvent before any sums can be recovered. Therefore, without the protection of a net contribution clause, a party could be pursued for the whole of the loss and have no practical way of reducing its liability, even if other parties were also at fault.

Background

The case related to works carried out to a house in Putney, purchased by Mr and Mrs West (the “Claimants”) in 2005. The Claimants planned to undertake various works to the property and engaged the architect Ian Finley & Associates (the “Defendant”). The parties

Key facts:

- The Court of Appeal overturned the TCC’s decision and enforced a net contribution clause, reducing the damages payable by an architect.
- The clause operated to limit the architect’s liability to the sums which it would be just and equitable for him to pay, having regard to the extent of his responsibility and that of other parties for the same loss.
entered into an appointment in February 2006 (the “Appointment”) and the Claimants subsequently appointed a number of other consultants, contractors and specialists in relation to various aspects of the works.

The Appointment was for “Normal Architectural Service as per RIBA Conditions” and was amended by various particular provisions. The Appointment included a clause limiting the Defendant’s liability, included the net contribution provisions as follows (which did not contain all the elements more commonly seen, for example in RIBA’s own standard form):

“Our liability for loss or damage will be limited to the amount that it is reasonable for us to pay in relation to the contractual responsibilities of other consultants, contractors and specialists appointed by you.”

A main contractor was subsequently appointed to carry out the works. Some time after completion of the remedial works, the main contractor became insolvent and the Claimant pursued no claim against it.

Following completion of the works, a number of defects became apparent and extensive remedial works were carried out, paid for by the Claimants. The Claimants commenced proceedings against the Defendant, alleging negligence in its failure to notice or remedy the various defects. At first instance, the TCC awarded the Claimants damages of £650,000, together with considerable interest.

Original decision

The Court held that the Defendant was liable for the defects and, in order to assess the extent of the damages payable, considered the net contribution clause.

A key consideration was the meaning of the words used in the net contribution clause. The Court had found that, contrary to the Claimants’ submissions, the clause was not “unfair”. It was not contrary to the requirement of good faith, and did not cause a significant imbalance in the parties’ rights and obligations (as would have been required under the UTCCR) and was, in principle at least, enforceable.

However, the scope of the clause was disputed. In particular, did the words “other consultants, contractors and specialists” include the main contractor (as argued by the Defendant), or relate only to the other parties appointed by the Claimant.

In light of the apparent uncertainty in the clause, the Court held that, pursuant to the UTCCR, the clause should be given the meaning most favourable to the consumer, in this case the Claimants. No apportionment of liability was made and the Defendant was held liable for the whole of the damages claimed.

Court of Appeal decision
The Court of Appeal started with the first consideration in any construction exercise, by looking at the normal meaning of the words used. The Court of Appeal did not accept that there was any ambiguity, finding the meaning of the words to be “crystal clear”. The clause limited the Defendant’s liability to the amount it was reasonable for it to pay, having regard to “the contractual responsibility of other consultants, contractors and specialists appointed by [the Claimants]”. There was no limitation on “others”, which therefore referred to any third parties appointed by the Claimants, including the main contractor subsequently appointed, notwithstanding the Defendant’s involvement in the appointment.

The Court of Appeal considered that the words used had a clear meaning and that there was nothing in the relevant factual matrix to lead to a conclusion that the parties had somehow used the wrong words to record their agreement.

Having found that the net contribution clause was sufficiently clear, the Court of Appeal went on to consider the questions of unfairness (by reference to any significant imbalance in the parties’ rights and the requirement to act in good faith) under the UTCCR and reasonableness under The Unfair Contract Terms Act 1977 (“UCTA”).

Having considered the guidance and authorities in relation to the UTCCR, including Director General of Fair Trading v. First National Bank plc [2002] 1 AC 481, the Court of Appeal concluded that inclusion of the net contribution clause was not “unfair”.

Although the clause did create an imbalance, this was not significant in the circumstances and did not tilt the parties’ rights and obligations significantly in favour of the Defendant (noting that the use of such clauses are common in RIBA standard forms, that the use of the clause would not be unusual in a commercial contract and that it was the Claimant who ultimately took the decision as to which main contractor to appoint).

Although the clause was not individually negotiated (or drawn expressly to the attention of the Claimants), the Court found that the parties were in an equal bargaining position and, considering all the factors, the balance lay in favour of the inclusion of the clause not being unfair.

Having found the clause not to be unfair, the Court went on to consider whether it was unreasonable, pursuant to the provisions of UCTA. UCTA is potentially applicable to both consumers and to businesses, where dealing on another party’s written standard terms. In those circumstances, a party may only exclude liability for its breaches so far as the contract term satisfies the requirement of reasonableness. This means that the term must be a fair and reasonable one to be included in the contract, having regard to the relevant circumstances.

The Court of Appeal considered the various factors, including the bargaining position of the parties, the Claimants’ knowledge of the
clause (it was included prominently on the third page of the document) and the lack of any particular conditions attaching to the net contribution clause (such as a time limit or similar), as well as those considered under the UTCCR, and concluded that the net contribution clause satisfied the requirement of reasonableness.

In all the circumstances, the net contribution clause was therefore enforceable by the Defendant to limit its liability.

**Application of the net contribution clause**

The Court of Appeal considered that the amount it would be reasonable for the Defendant to pay should be looked at in the same way as a contribution under the Civil Liability (Contribution) Act 1978, given the similarity between the wording of the clause and the Act. Section 2(1) of the Act provides that the amount recoverable shall be “such as may be found by the court to be just and equitable having regard to that person’s responsibility for the damage in question”. The Court of Appeal went on to note, significantly in this case, that this exercise does not consider the ability of any other parties to pay any sum which might be claimed.

The matter has been remitted to the judge in the original hearing to consider the amount it was reasonable, in all the circumstances, for the Defendant to have paid (taking into account the contractual responsibilities of the main contractor).

**Conclusion**

The judgment is very welcome news for consultants and their insurers, demonstrating that net contribution clauses will be enforced even, as was the case here, where one of the other parties responsible for the loss has become insolvent. Provided that the net contribution clause is clearly worded, and is not unfair or unreasonable, it will be enforced by the Courts. Although this case dealt with a consumer client and considered the provisions of the UTCCR, it is also instructive on wider basis – parties should ensure that their net contribution clauses are clearly drafted and, where dealing with written standard terms, satisfy the requirement of reasonableness.

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