7. Exemption clauses and unfair contract terms

Generally, an exemption clause is defined as a term in a contract or notice that either seeks to exclude liability or remedies for breach of contract and/or negligence (referred to as ‘exclusion clauses’ in this casebook), or seeks to limit that liability to a specified sum (referred to as ‘limitation clauses’).

7.1 The general approach to exemption clauses

There are distinct advantages in using exemption clauses to allocate risk, e.g. the avoidance of duplicate insurance and lower pricing. However, at common law, the courts were very concerned to protect a party against an exemption clause imposed without negotiation by a party who had superior bargaining power. The courts could achieve this by finding that the clause had not been incorporated as a term of the contract, e.g. *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 163 (see page 235, Chapter 6, section 6.3.1.3), although this option was not available if the weaker party had signed a standard form contract without reading it: *L'Estrange v Graucob Ltd* [1934] 2 KB 394 (see page 227,
Chapter 6, section 6.2.2). More frequently, they resorted to construing the clause so that it did not provide protection for the stronger party in the circumstances that had occurred. To achieve this, the courts often construed the clause artificially: Hollier v Rambler Motors (AMC) Ltd [1972] 2 QB 71 (see page 296, section 7.3.2.2.2).

Since the Unfair Contract Terms Act (UCTA) 1977, the Unfair Terms in Consumer Contracts Regulations (UTCCR) 1999, SI 1999/2083 (now revoked) and their subsequent replacement legislative protection contained in Part 2 of the Consumer Rights Act (CRA) 2015, it is no longer necessary for such judicial restrictive approaches to incorporation and construction. Lord Diplock stated in Photo Production Ltd v Securicor Transport Ltd [1980] AC 827, 851:

My Lords, the reports are full of cases in which what would appear to be very strained constructions have been placed upon exclusion clauses, mainly in what today would be called consumer contracts and contracts of adhesion. As Lord Wilberforce has pointed out, any need for this kind of judicial distortion of the English language has been banished by Parliament’s having made these kinds of contracts subject to the Unfair Contract Terms Act 1977. In commercial contracts negotiated between businessmen capable of looking after their own interests and of deciding how risks inherent in the performance of various kinds of contract can be most economically borne (generally by insurance), it is, in my view, wrong to place a strained construction upon words in an exclusion clause which are clear and fairly susceptible of one meaning only.

7.2 Requirements that must be satisfied before an exemption clause can be relied upon

To rely on an exemption clause as a defence to liability that would otherwise exist, a party must show that:

(a) it has been incorporated as a term of the contract (see the discussion of incorporation of terms at pages 227–46);
(b) on its natural and ordinary meaning, it covers the event(s) that has/have occurred (see section 7.3); and
(c) it is not rendered unenforceable by the applicable legislation, i.e. UCTA 1977 (B2B—business to business—contracts) or the CRA 2015 (B2C—trader and consumer—contracts) (see from page 305, sections 7.4 and 7.5).

7.3 Construction: on its natural and ordinary meaning, the clause covered what happened
7. Exemption clauses and unfair contract terms

Before UCTA 1977, the courts adopted a restrictive and often artificial approach to construction to protect the weaker party. Lord Denning admitted this in the Court of Appeal in *George Mitchell (Chester Hall) Ltd v Finney Lock Seeds Ltd* [1983] QB 284, at p. 297:

**The heyday of freedom of contract**

None of you nowadays will remember the trouble we had—when I was called to the Bar—with exemption clauses. They were printed in small print on the back of tickets and order forms and invoices. They were contained in catalogues or timetables. They were held to be binding on any person who took them without objection. No one ever did object. He never read them or knew what was in them. No matter how unreasonable they were, he was bound. All this was done in the name of ‘freedom of contract.’ But the freedom was all on the side of the big concern which had the use of the printing press. No freedom for the little man who took the ticket or order form or invoice. The big concern said, ‘Take it or leave it.’ The little man had no option but to take it. The big concern could and did exempt itself from liability in its own interest without regard to the little man. It got away with it time after time. When the courts said to the big concern, ‘You must put it in clear words,’ the big concern had no hesitation in doing so. It knew well that the little man would never read the exemption clauses or understand them. (p. 291)

It was a bleak winter for our law of contract. It is illustrated by two cases, *Thompson v London, Midland and Scottish Railway Co.* [1930] 1 KB 41 (in which there was exemption from liability, not on the ticket, but only in small print at the back of the timetable, and the company were held not liable) and *L'Estrange v F. Graucob Ltd* [1934] 2 KB 394 (in which there was complete exemption in small print at the bottom of the order form, and the company were held not liable).

**The secret weapon**

Faced with this abuse of power—by the strong against the weak—by the use of the small print of the conditions—the judges did what they could to put a curb upon it. They still had before them the idol, ‘freedom of contract.’ They still knelt down and worshipped it, but they concealed under their cloaks a secret weapon. They used it to stab the idol in the back. This weapon was called ‘the true construction of the contract.’ They used it with great skill and ingenuity. They used it so as to depart from the natural meaning of the words of the exemption clause and to put upon them a strained and unnatural construction. In case after case, they said that the words were not strong enough to give the
7. Exemption clauses and unfair contract terms

big concern exemption from liability; or that in the circumstances the big concern was not entitled to rely on the exemption clause ...

When examining many of the cases that follow, remember that the courts are unlikely to adopt such a restrictive approach to the question of construction when legislative regulation is available.

7.3.1 Contra proferentem

Any ambiguity in an exemption clause will be resolved against the party seeking to rely upon it.

Houghton v Trafalgar Insurance Co. Ltd

[1954] 1 QB 247 (CA)

A car insurance policy excluded liability for damage 'caused or arising whilst the car is conveying any load in excess of that for which it was constructed'. At the time of the accident, six people were in a car with seating accommodation for five; the insurers denied liability, claiming that this was a load in excess of that for which the car was constructed.

**Held:** The word 'load' covered only cases in which there was a specified weight that must not be exceeded, as in the case of lorries or vans.

ROMER LJ: I think that it would be most regrettable if a provision of this kind were held to have the force for which the defendants contend. It would be a serious thing for a motorist involved in a collision if he were told that the particular circumstances of the accident excluded him from the benefit of the policy. I think that any clause or provision that purports to have that effect ought to be clear and unambiguous so that the motorist knows exactly where he stands. This provision is neither clear nor unambiguous. If applied to a private motor-car I have not the least idea what it means ...

 Notes

1. As Romer LJ appears to be suggesting, policy reasons may also have caused the Court of Appeal to reject the insurers’
7. Exemption clauses and unfair contract terms

suggested interpretation, which would have had a devastating effect on the ability of innocent third parties to recover on car insurance policies in those circumstances.

2. In *Andrews Brothers (Bournemouth) Ltd v Singer & Co. Ltd* [1934] 1 KB 17, the exemption covered all implied obligations, but the Court of Appeal held that the defendants could not rely on this as exempting them from liability for breach of the express obligation that the car be ‘new’.

3. The contra proferentem rule is expressly incorporated in the Consumer Rights Act (CRA) 2015, s. 69.

69 Contract terms that may have different meanings

(1) If a term in a consumer contract, or a consumer notice, could have different meanings, the meaning that is most favourable to the consumer is to prevail.

7.3.2 Liability for negligence

It can be difficult to grasp the concept that, in an action in negligence, the defendant may seek to rely on an exemption clause in a contract to which he is a party to protect himself (as to the position where a third party seeks to do this, see Chapter 11).

Traditionally, the courts’ approach has been to limit the scope of exclusion clauses and construe them so that they cover only contractual liability unless the clause expressly extends to negligence.

In *Canada Steamship Lines Ltd v R* [1952] AC 192, 208, Lord Morton of Henryton laid down a construction test to ascertain whether the clause covers negligence liability:

Their Lordships think that the duty of a court in approaching the consideration of such clauses may be summarised as follows:—

(1) If the clause contains language which expressly exempts the person in whose favour it is made (hereafter called ‘the proferens’) from the consequence of the negligence of his own servants, effect must be given to that provision …

(2) If there is no express reference to negligence, the court must consider whether the words used are wide enough, in their ordinary meaning, to cover negligence on the part of the servants of the proferens. If a doubt arises at this point, it must be resolved against the proferens …
7. Exemption clauses and unfair contract terms

(3) If the words used are wide enough for the above purpose, the court must then consider whether ‘the head of damage may be based on some ground other than that of negligence,’ to quote again Lord Greene, in the *Alderslade* case [1945] KB 189. The ‘other ground’ must not be so fanciful or remote that the proferens cannot be supposed to have desired protection against it; but subject to this qualification, which is no doubt to be implied from Lord Greene’s words, the existence of a possible head of damage other than that of negligence is fatal to the proferens even if the words used are prima facie wide enough to cover negligence on the part of his servants …

7.3.2.1 The first possibility is that the clause expressly refers to negligence or a synonym of negligence

Most clauses will use more general words, but the following case concerned a clause that covered negligence liability, because the words ‘neglect or default’ were synonymous with negligence. If the clause expressly refers to negligence, it will cover negligence liability and any other liability that may arise on the facts, e.g. breach of statutory duty or strict contractual liability.

**Monarch Airlines Ltd v London Luton Airport Ltd**

[1997] CLC 698

Loose paving blocks had damaged one of the claimant airline’s aircraft as it was preparing to take off from the airport. When the claimant sued to recover damages for negligence and/or breach of duty under s. 2 of the Occupiers’ Liability Act 1957, the defendant sought to rely on clause 10 of its standard conditions, which excluded the liability of the airport, its servants, and agents for any damage to aircraft ‘arising or resulting directly or indirectly from any act, omission, neglect or default … unless done with intent to cause damage or recklessly and with knowledge that damage would probably result’. The claimant submitted that this clause did not cover the liability that had occurred since, applying the test in *Canada Steamship v R*, clause 10 did not cover negligence liability.

**Held (Clarke J):** The clause excluded liability for negligence and any breach of statutory duty unless the negligence or breach was caused either with intent to cause damage or recklessly and with knowledge that damage would probably result. The words ‘neglect or default’ were synonymous with negligence. The clause therefore passed Lord Morton’s first test.
7. Exemption clauses and unfair contract terms

7.3.2.2 The second possibility requires that the words be wide enough to cover negligence

In Lamport & Holt Lines Ltd v Coubro & Scrutton (M & I) Ltd, The Raphael [1982] 2 Lloyd’s Rep 42, the words ‘any act or omission’ were held to be words that were wide enough to cover negligence.

7.3.2.2.1 Is there any other liability arising on these facts?

Provided the words are wide enough to cover negligence, we can then ask whether there is any other liability that exists on these facts, e.g. breach of a strict (or absolute) contractual obligation. If so, the clause is confined to this alternative liability and cannot apply to cover the liability in negligence.

White v John Warwick & Co. Ltd

[1953] 1 WLR 1285 (CA)

The claimant contracted with the defendants for the hire of a tradesman’s tricycle. The tricycle supplied under the agreement had a defective saddle. The claimant was thrown off the tricycle when the saddle tipped up, and was injured. Clause 11 of their agreement provided that the defendants would not be liable ‘for any personal injuries to the riders of the machines hired’. The claimant sought damages, alleging that: (i) the defendants were strictly liable in contract in supplying a tricycle that was not reasonably fit for the purpose for which it was required; and (ii) the defendants were negligent as they had failed to take care to ensure that the tricycle supplied was in a proper state of repair and in working condition. Counsel for the claimant argued that although clause 11 might apply to the breach of contract claim, it did not—and could not—apply to the negligence. The Court of Appeal agreed.

Held: The clause applied only to exempt the defendants from contractual liability.

(p. 294)

DENNING LJ: In this type of case two principles are well settled. The first is that if a person desires to exempt himself from a liability which the common law imposes on him, he can only do so by a contract freely and deliberately entered into by the injured party in words that are clear beyond the possibility of misunderstanding. The second is: if there are two possible heads of liability on the part of defendant, one for negligence, and the other a strict liability, an exemption clause will be construed, so far as possible, as exempting the defendant only
from his strict liability and not as relieving him from his liability for negligence.

In the present case, there are two possible heads of liability on the defendants, one for negligence, the other for breach of contract. The liability for breach of contract is more strict than the liability for negligence. The defendants may be liable in contract for supplying a defective machine even though they were not negligent. (See *Hyman v Nye* (1881) 6 QBD 685). In these circumstances, the exemption clause must, I think, be construed as exempting the defendants only from their liability in contract, and not from their liability for negligence.

Thus the clause could not operate in a claim based on negligence. This decision pre-dates the legislative regulation. Nowadays, even if the clause is wide enough to cover negligence, it will still need to satisfy either s. 2 UCTA 1977 (see page 313, section 7.4.3) in the B2B context or ss. 62 and 65 CRA 2015 (see pages 334 and 335, section 7.5.3). Given the scope of this protection, e.g. not permitting reliance on any clause that excludes or restricts liability for death or personal injury resulting from negligence, it may no longer be necessary to adopt such a restrictive approach to construction and negligence liability to protect the weak.

### 7.3.2.2.2 Is negligence the only liability arising on the facts?

Where the only basis of liability is negligence, the courts are more willing to construe the clause to cover that negligence.

**Alderslade v Hendon Laundry Ltd**

*[1945] 1 KB 189 (CA)*

The claimant left ten large Irish linen handkerchiefs with the defendants to be washed. The laundry lost the handkerchiefs, but in an action by the claimant for damages for £2 1s. 5½d. (the cost of replacement handkerchiefs), the defendants sought to rely on condition 3 of the terms on which the handkerchiefs had been accepted. This provided that ‘[t]he maximum amount allowed for lost
7. Exemption clauses and unfair contract terms

Held: The only liability that could arise from the loss of the handkerchiefs by the defendants was by establishing that the defendants were negligent. They owed only a duty to take reasonable care of the handkerchiefs, so that there could be no strict liability for such loss. The condition could therefore be applied to limit that negligence liability and the damages payable to the claimant.

LORD GREENE MR: It was argued before us for the defendants that the clause did apply and was effective to limit liability for lost articles; and reliance was placed on a well-known line of authority dealing with clauses of this description. The effect of those authorities can I think be stated as follows: where the head of damage in respect of which limitation of liability is sought to be imposed by such a clause is one which rests on negligence and nothing else, the clause must be construed as extending to that head of damage, because it would otherwise lack subject-matter. Where, on the other hand, the head of damage may be based on some other ground than that of negligence, the general principle is that the clause must be confined in its application to loss occurring through that other cause, to the exclusion of loss arising through negligence. The reason is that if a contracting party wishes in such a case to limit his liability in respect of negligence, he must do so in clear terms in the absence of which the clause is construed as relating to a liability not based on negligence. A common illustration of the principle is to be found in the case of common carriers. A common carrier is frequently described, though perhaps not quite accurately, as an insurer, and his liability in respect of articles entrusted to him is not necessarily based on negligence. Accordingly if a common carrier wishes to limit his liability for lost articles and does not make it quite clear that he is desiring to limit it in respect of his liability for negligence, then the clause will be construed as extending only to his liability on grounds other than negligence. If, on the other hand, a carrier not being a common carrier, makes use of such a clause, then unless it is construed so as to cover the case of negligence there would be no content for it at all seeing that his only obligation is to take reasonable care. That, broadly speaking, is the principle which falls to be applied in this case.

It was argued by counsel for the plaintiff that the clause must be construed in the present case so as to exclude loss by negligence ... It was said that the loss of a customer’s property might take place for one of two reasons, namely, negligence and mere breach of contract, and that in the absence of clear words
referring to negligence, loss through negligence cannot be
taken to be covered by the clause. In my opinion that argument
fails. It is necessary to analyse the legal relationship between
the customer and the defendants. What I may call the hard core
of the contract, the real thing to which the contract is directed,
is the obligation of the defendants to launder. That is the
primary obligation. It is the contractual obligation which must
be performed according to its terms, and no question of taking
due care enters into it. The defendants undertake, not to
exercise due care in laundering the customer’s goods, but to
launder them, and if they fail to launder them it is no use their
saying, ‘We did our best, we exercised due care and took
reasonable precautions, and we are very sorry if as a result the
linen is not properly laundered.’ That is the essence of the
contract, and in addition there are certain ancillary obligations
into which the defendants enter if they accept goods from a
customer to be laundered. The first relates to the safe custody
of the goods while they are in the possession of the defendants.
The customer’s goods may have to wait for a time in the
laundry premises to be washed, and while they are so waiting
there is an obligation to take care of them, but it is in my
opinion not the obligation of an insurer but the obligation to
take reasonable care for the protection of the goods. If while
they are waiting to be washed in the laundry a thief, through no
fault of the defendants, steals them, the defendants are not
liable. The only way in which the defendants could be made
liable for the loss of articles awaiting their turn to be washed
would, I think, quite clearly be if it could be shown that they
had been guilty of negligence in performing their duty to take
care of the goods. That is one ancillary obligation which is
inherent in a contract of this kind. Another relates to the
delivery of the goods. The laundry company in most cases, and
indeed in this case, make a practice of delivering the goods to
the customer, and in the ordinary way the customer expects to
receive that service. But what is the precise obligation of the
laundry in respect of the return of the goods after the
laundering has been completed? In my opinion it stands on the
same footing as the other ancillary obligation that I have
mentioned, namely, the obligation to take reasonable care in
looking after and safeguarding the goods. It cannot I think be
suggested that the obligation of the laundry company in the
matter of returning the goods after they have been laundered is
the obligation of an insurer. To say that they have undertaken
by contract an absolute obligation to see that they are returned
seems to me to go against common sense. Supposing the
defendants are returning the goods by van to their customer
and while the van is on its way a negligent driver of a lorry
drives into it and overturns it with the result that it is set on fire
and the goods destroyed. No action would lie by the customer
for damages for the loss of those goods any more than it would
lie against any ordinary transport undertaking which
was not a common carrier. To hold otherwise would mean that
in respect of that clearly ancillary service the defendants were
undertaking an absolute obligation that the goods would,
whatever happened, be returned to the customer. It seems to
me that the only obligation on the defendants in the matter of
returning the goods is to take reasonable care.

In the present case all that we know about the goods is that
they are lost. There seems to me to be no case of lost goods in
respect of which it would be necessary to limit liability, unless it
be a case where the goods are lost by negligence. Goods sent to
the laundry will not be lost in the act of washing them. On the
other hand, they may be lost while they are in the custody of
the defendants before washing or after washing has been
completed. They may be lost in the process of returning them to
the customer after they have been washed, but in each of those
two cases, if my view is right, the obligation of the defendants is
an obligation to take reasonable care and nothing else.
Therefore, the claim of a customer that the defendants are
liable to him in respect of articles that have been lost must, I
think, depend on the issue of due care on their part. If that be
right, to construe this clause, so far as it relates to loss, in such
a way as to exclude loss occasioned by lack of proper care,
would be to leave the clause so far as loss is concerned—I say
nothing about damage—without any content at all. The result is
in my opinion is that the clause must be construed as applying
to the case of loss through negligence ...

Notes

1. The laundry company supplies a service in the course of a
business it impliedly undertakes (or includes a term) whereby
the service must be performed ‘with reasonable care and
skill’ (Supply of Goods and Services Act 1982, s. 13 (B2B), or
CRA 2015, s. 49 (B2C)). Therefore it seems that Lord Greene’s
identification of a strict obligation to launder properly might
need to be amended in the light of this provision. However, in
the B2B context which is still based on the implication of terms
(as opposed to entrenched terms in the CRA 2015), s. 16 of the
1982 Act leaves open the possibility that a court may imply
terms that are stricter than the qualified standard in s. 13. Other
obligations, such as not losing the handkerchiefs, are clearly
qualified (i.e. the duty owed is one of reasonable care and skill),
7. Exemption clauses and unfair contract terms

and the laundry company is negligent if it fails to exercise reasonable care and skill to prevent loss.

2. Lord Greene indicated that it was an automatic conclusion that, where negligence is the only liability that can arise, the exemption clause must be construed as applying to it. However, this was not accepted by the Court of Appeal in the next case.

Hollier v Rambler Motors (AMC) Ltd

[1972] 2 QB 71 (CA)

The claimant’s car was being repaired at the defendants’ garage when it was damaged by a fire caused by the defendants’ negligence. The claimant claimed damages for breach of the implied term that the defendants would take reasonable care of his car. The defendants sought to rely on a clause in their standard form for repair, which provided that: ‘The Company is not responsible for damage caused by fire to customers’ cars on the premises.’

Held: The clause had not been incorporated because there was not a consistent course of dealing (see page 242, Chapter 6, section 6.3.2). It was also held that, in any event, the language of this clause did not exclude liability for the defendants’ negligence, but was merely a ‘warning’ that the defendants would not be liable for fire damage that was not attributable to their own negligence.

SALMON LJ: It is well settled that a clause excluding liability for negligence should make its meaning plain on its face to any ordinarily literate and sensible person. The easiest way of doing that, of course, is to state expressly that the garage, tradesman or merchant, as the case may be, will not be responsible (p. 297) for any damage caused by his own negligence. No doubt merchants, tradesmen, garage proprietors and the like are a little shy of writing in an exclusion clause quite so bluntly as that. Clearly it would not tend to attract customers, and might even put many off. I am not saying that an exclusion clause cannot be effective to exclude negligence unless it does so expressly, but in order for the clause to be effective the language should be so plain that it clearly bears that meaning. I do not think that defendants should be allowed to shelter behind language which might lull the customer into a false sense of security by letting him think—unless perhaps he happens to be a lawyer—that he would have redress against the man with whom he was dealing for any damage which he, the customer, might suffer by the negligence of that person.
The principles are stated by Scrutton L.J. with his usual clarity in *Rutter v. Palmer* [1922] 2 K.B. 87, 92:

For the present purposes a rougher test will serve. In construing an exemption clause certain general rules may be applied: First the defendant is not exempted from liability for the negligence of his servants unless adequate words are used; secondly, the liability of the defendant apart from the exempting words must be ascertained; then the particular clause in question must be considered; and if the only liability of the party pleading the exemption is a liability for negligence, the clause will more readily operate to exempt him.

Scrutton L.J was far too great a lawyer; and had far too much robust common sense, if I may be permitted to say so, to put it higher than that ‘if the only liability of the party pleading the exemption is a liability for negligence, the clause will more readily operate to exempt him.’ He does not say that ‘if the only liability of the party pleading the exemption is a liability for negligence, the clause will necessarily exempt him.’ …

*Alderslade v Hendon Laundry Ltd* [1945] 1 KB 189 … was a case where negligence was not expressly excluded. The question was: what do the words mean? I have no doubt that they would mean to the ordinary housewife who was sending her washing to the laundry that, if the goods were lost or damaged in the course of being washed through the negligence of the laundry, the laundry would not be liable for more than 20 times the charge made for the laundering. I say that for this reason. It is, I think, obvious that when a laundry loses or damages goods it is almost invariably because there has been some neglect or default on the part of the laundry. I think that the ordinary sensible housewife, or indeed anyone else who sends washing to the laundry, who saw that clause must have appreciated that almost always goods are lost or damaged because of the laundry’s negligence, and therefore this clause could apply only to limit the liability of the laundry, when they were in fault or negligent.

But [counsel for the defendants] has drawn our attention to the way in which the matter was put by Lord Greene MR in delivering the leading judgment in this court, and he contends that Lord Greene MR was in fact making a considerable extension to the law …

I do not think that Lord Greene MR was intending to extend the law in the sense for which [counsel for the defendants] contends. If it were so extended, it would make the law entirely
artificial by ignoring that rules of construction are merely our
guides and not our masters; in the end you are driven back to
construing the clause in question to see what it means ... The
words are: 'The company is not responsible for damage caused
by fire to customers’ cars on the premises.' What would that
mean to any ordinarily literate and sensible car owner? I do not
suppose that any such, unless he is a trained lawyer, has an
intimate or indeed any knowledge of the liability of bailees in
law. If you asked the ordinary man or woman: ‘Supposing you
send your car to the garage to be repaired, and there is a fire,
would you suppose that the garage would be liable?’ I should be
surprised if many of them did not answer, quite wrongly: ‘Of
course they are liable if there is a fire.’ Others might be more
cautious and say: ‘Well, I had better ask my solicitor,’ or, ‘I do
not know. I suppose they may well be liable.’ That is the crucial
difference, to my mind, between the present case and
Alderslade v Hendon Laundry Ltd ... [H]ere I think the ordinary
man or woman would be ... surprised and horrified to learn that
if the garage was so negligent that a fire was (p. 298) caused
which damaged their car, they would be without remedy
because of the words in the condition. I can quite understand
that the ordinary man or woman would consider that, because
of these words, the mere fact that there was a fire would not
make the garage liable. Fires can occur from a large variety of
causes, only one of which is negligence on the part of the
occupier of the premises, and that is by no means the most
frequent cause. The ordinary man would I think say to himself:
‘Well, what they are telling me is that if there is a fire due to
any cause other than their own negligence they are not
responsible for it.’ To my mind, if the defendants were seeking
to exclude their responsibility for a fire caused by their own
negligence, they ought to have done so in far plainer language
than the language here used ...

Question

This case was severely criticized for its artificial approach to
construction of the clause. Do you think that this case would be
delected in the same way today? If the clause is held to cover
negligence, it would be subject to the unfairness test in s. 62 CRA
2015. Section 62(4) CRA 2015 provides that ‘a term is unfair if,
contrary to the requirement of good faith, it causes a significant
imbalance in the parties’ rights and obligations under the contract to
the detriment of the consumer’. Do you think that the clause in this
case would satisfy this s. 62(4) test? (See pages 334–5, section 7.5.3.)
7. Exemption clauses and unfair contract terms

NOTE

The Canada Steamship principles need to be understood in the light of general construction principles. In the speeches of the House of Lords in HIH Casualty & General Insurance Ltd v Chase Manhattan Bank [2003] UKHL 6, [2003] 1 All ER (Comm) 349, their Lordships had confirmed that Lord Morton’s guidelines would need to be read in light of the more contextual approach to contractual interpretation consequent on the principles developed in Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896 (see page 273, Chapter 6, section 6.5.1). In HIH Casualty Lord Bingham stated, at [111], that Lord Morton:

was giving helpful guidance on the proper approach to interpretation and not laying down a code. The passage does not provide a litmus test which, applied to the terms of the contract, yields a certain and predictable result. The courts’ task of ascertaining what the particular parties intended in their particular commercial context, remains.

Following the clarification of the interpretation process as an ‘unitary exercise’ in Wood v Capita Insurance Services Ltd [2017] UKSC 24, [2017] AC 117 (see page 280, Chapter 6, section 6.5.4), the words used by the parties are still the starting point of interpretation but those words nevertheless have to be assessed in the commercial context of the contract.

Although important, Lord Morton’s guidelines are no more than guidelines and are not to be applied mechanistically (Lictor Anstalt v MIR Steel UK Ltd [2012] EWCA Civ 1397, [2013] 2 All ER (Comm) 54, [2013] CP Rep 7). Specifically, they are not to be applied in a way that would produce a result at odds with the parties’ intentions in the context of the relevant background. Nevertheless, clear words are still required to exclude a person’s liability for the consequences of their own negligence and the starting point to determine this must be the words the parties have used. Furthermore, doubts as to their continuing application continue to accrue. Most recently, in Persimmon Homes Ltd v Ove Arup & Partners Ltd [2017] EWCA Civ 373, [2017] BLR 417, Jackson LJ stated that those guidelines are now confined to indemnity clauses (at [56]).

7.3.3 Limitation clauses
7. Exemption clauses and unfair contract terms

Ailsa Craig Fishing Co. Ltd v Malvern Fishing Co. Ltd

[1983] 1 WLR 964 (HL)

Securicor had agreed to provide a security service in Aberdeen harbour for the fishing boats of the members of an association that were berthed there. Ailsa Craig’s vessel fouled another boat in the harbour and sank. Clause 2(f) purported to limit Securicor’s liability to £1,000. Ailsa Craig claimed damages against Securicor, alleging that the loss was caused by breach of contract and/or negligence. The trial judge awarded damages of £55,000. Securicor appealed, alleging that condition 2(f) applied.

**Held:** The limitation clause operated to limit liability to £1,000. Limitation clauses were not to be construed by the exacting standards applicable to exclusion clauses. This clause was clear and unambiguous, it was therefore wide enough to cover liability in negligence.

LORD WILBERFORCE: Whether a clause limiting liability is effective or not is a question of construction of that clause in the context of the contract as a whole. If it is to exclude liability for negligence, it must be most clearly and unambiguously expressed, and in such a contract as this, must be construed contra proferentem. I do not think that there is any doubt so far. But I venture to add one further qualification, or at least clarification: one must not strive to create ambiguities by strained construction, as I think that the appellants have striven to do. The relevant words must be given, if possible, their natural, plain meaning. Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion: this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives, and possibly also the opportunity of the other party to insure.

LORD FRASER: In my opinion these principles [per Lord Morton of Henryton in Canada Steamship Lines Ltd v R [1952] AC 192] are not applicable in their full rigour when considering the effect of clauses merely limiting liability. Such clauses will of course be read contra proferentem and must be clearly expressed, but there is no reason why they should be judged by the specially exacting standards which are applied to exclusion and indemnity clauses. The reason for imposing such standards on these clauses is the inherent improbability that the other party to a contract including such a clause intended to release the proferens from a liability that would otherwise fall upon him. But there is no such high degree of improbability that he
would agree to a limitation of the liability of the proferens, especially when ... the potential losses that might be caused by the negligence of the proferens or its servants are so great in proportion to the sums that can reasonably be charged for the services contracted for. It is enough in the present case that the clause must be clear and unambiguous.

Is this special construction of limitation clauses justifiable?

The legislation applies equally to limitation and exclusion clauses, and it may simply be that many limitation clauses are more likely to satisfy the reasonableness requirement in s. 11 UCTA 1977 or the test of fairness in s. 62 CRA 2015. The High Court of Australia, in Darlington Futures Ltd v Delco Australia Pty Ltd (1986) 161 CLR 500, (1986) 61 ALJR 76, considered this distinction in construction to be unsupportable, since if the limitation clause were to set the figure for recovery at a very low level, its effects would be much the same as those applicable to total exclusion clauses.

7.3.4 Inconsistent terms

If an exemption clause is inconsistent with another express term of the contract or an oral undertaking given at or before the time of contracting, then the exemption clause is overridden by that term or undertaking.

Mendelssohn v Normand Ltd

[1970] 1 QB 177 (CA)

The claimant was told by the parking attendant that the rules required the car to be left unlocked. The claimant explained that he had a suitcase in the car containing valuables, and the attendant agreed to lock the car as soon as he had moved it. The claimant was then given a ticket exempting the garage from responsibility for loss or damage to vehicles or their contents, however caused. On his return, the claimant found the car unlocked and later discovered that his suitcase was missing. Were the defendants liable for the loss of the suitcase?

Held: The defendants were liable, since the attendant’s promise (to lock up the car, which implied that he would see that the contents
7. Exemption clauses and unfair contract terms

were safe) took priority over the printed condition, because the printed condition was repugnant to that express promise.

LORD DENNING MR: Such a statement is binding on the company. It takes priority over any printed condition. There are many cases in the books when a man has made, by word of mouth, a promise or a representation of fact, on which the other party acts by entering into the contract. In all such cases the man is not allowed to repudiate his representation by reference to a printed condition, see Couchman v Hill [1947] KB 554; Curtis v Chemical Cleaning & Dyeing Co. [1951] 1 KB 805; and Harling v Eddy [1951] 2 KB 739; nor is he allowed to go back on his promise by reliance on a written clause, see City and Westminster Properties (1934) Ltd v Mudd [1959] Ch 129, 145 by Harman J. The reason is because the oral promise or representation has a decisive influence on the transaction—it is the very thing which induces the other to contract—and it would be most unjust to allow the maker to go back on it. The printed condition is rejected because it is repugnant to the express oral promise or representation. As Devlin J said in Firestone Tyre and Rubber Co. Ltd v Vokins & Co. Ltd [1951] 1 Lloyd’s Rep 32, 39: ‘It is illusory to say: “We promise to do a thing, but we are not liable if we do not do it”.’ To avoid this illusion, the law gives the oral promise priority over the printed clause.

NOTE

J. Evans & Son (Portsmouth) v Andrea Merzario Ltd [1976] 1 WLR 1078 (see page 220, Chapter 6, section 6.2.1.1) provides another example. The printed conditions gave the defendants complete freedom to decide the method of transportation of goods and exempted the defendants for loss of or damage to the goods. However, the claimants had been given an oral assurance that the containers would be stored below deck. The defendants were not entitled to rely upon the printed conditions to exempt them from liability for this breach, because this would render the oral promise illusory.
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7.3.5 Fundamental breach

A ‘fundamental’ breach is a serious breach that goes to the root of the contract. It may include so-called ‘breach of a fundamental term’, e.g. a breach of condition. A fundamental breach would be considered to be repudiatory. In the 1950s and early 1960s, as part of their restrictive approach to construction, the courts took particular exception to the use of an exemption clause to protect against liability where the breach in question was ‘fundamental’ and held, in a series of cases, that exemption clauses could not operate to exclude liability for such breaches. The courts used to consider that a repudiatory breach destroyed the contract and its terms, including any exemption clauses. However, this is clearly incorrect, since repudiatory breach offers only the option to terminate the contract, i.e. to discharge future obligations. In *Suisse Atlantique Société d’Armement Maritime SA v NV Rotterdamsche Kolen Centrale* [1967] 1 AC 361, the House of Lords held, *obiter*, that there was no such rule of law applicable to fundamental breaches. The House of Lords also considered that it was a question of construction whether an exemption clause covered a fundamental breach, or any breach, of contract.

The House of Lords confirmed the construction approach in the next case.

**Photo Production Ltd v Securicor Transport Ltd**

**[1980] AC 827 (HL)**

The claimants, factory owners, entered into a contract with the defendants whereby the defendants would patrol the factory at a cost of £8 15s. per week. The contract, on the defendants’ standard form, included the following clause:

> Under no circumstances shall the company [Securicor] be responsible for any injurious act or default by any employee of the company unless such act or default could have been foreseen and avoided by the exercise of due diligence on the part of the company as his employer; nor, in any event, shall the company be held responsible for (a) any loss suffered by the customer through burglary, theft, fire or any other cause, except insofar as such loss is solely attributable to the negligence of the company’s employees acting within the course of their employment …

A defendants’ employee patrolling the factory started a fire by discarding a lighted match. The flames spread destroying the factory, causing a loss of £615,000. The claimants claimed damages from the defendants. Applying the ‘fundamental breach rule’ the Court of Appeal held that the contract had been brought to an end, so that the
defendants were not able to rely on this clause as excluding their liability. The House of Lords allowed the defendants’ appeal.

**Held:**

(a) It was not good law to say that, on termination of a contract for a fundamental breach, the contract terms (including any exemption clauses) came to an end.

(b) The question of whether and to what extent an exemption clause was to be applied to any breach of contract was a question of construction of the contract.

(c) Normally, when the parties were bargaining on equal terms, they should be free to apportion the risks as they saw fit.

(d) On their true construction, the words of the exclusion clause covered deliberate acts, and therefore the defendants were relieved from responsibility for breach of their implied duty to operate with due regard to the safety of the premises.

LORD WILBERFORCE: It is first necessary to decide upon the correct approach to a case such as this where it is sought to invoke an exception or limitation clause in the contract. The approach of Lord Denning MR in the Court of Appeal was to consider first whether the breach was ‘fundamental.’ If so, he said, the court itself deprives the party of the benefit of an exemption or limitation clause ([1978] 1 WLR 856, 863). Shaw and Waller LJJ substantially followed him in this argument …

My Lords, whatever the intrinsic merit of this doctrine, as to which I shall have something to say later, it is clear to me that so far from following this House’s decision in the *Suisse Atlantique* it is directly opposed to it and that the whole purpose and tenor of the *Suisse Atlantique* was to repudiate it. The lengthy, and perhaps I may say sometimes indigestible speeches of their Lordships, are correctly summarised in the headnote—holding No. 3 [1967] 1 AC 361, 362—‘That the question whether an exceptions clause was applicable where there was a fundamental breach of contract was one of the true construction of the contract.’ That there was any rule of law by which exceptions clauses are eliminated, or deprived of effect, regardless of their terms, was clearly not the view of Viscount Dilhorne, Lord Hodson, or of myself. The passages invoked for the contrary view of a rule of law consist only of short extracts from two of the speeches—on any view a minority. But the case for the doctrine does not even go so far as that. Lord Reid, in my respectful opinion, and I recognise that I may not be the best judge of this matter, in his speech read as a whole, cannot be claimed as a supporter of a rule of law … I am convinced that, with the possible exception of Lord Upjohn whose critical passage, when read in full,
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is somewhat ambiguous, their Lordships, fairly read, can only be taken to have rejected those suggestions for a rule of law which had appeared in the Court of Appeal and to have firmly stated that the question is one of construction, not merely of course of the exclusion clause alone, but of the whole contract.

Much has been written about the Suisse Atlantique case. Each speech has been subjected to various degrees of analysis and criticism, much of it constructive. Speaking for myself I am conscious of imperfections of terminology, though sometimes in good company. But I do not think that I should be conducing to the clarity of the law by adding to what was already too ample a discussion a further analysis which in turn would have to be interpreted. I have no second thoughts as to the main proposition that the question whether, and to what extent, an exclusion clause is to be applied to a fundamental breach, or a breach of a fundamental term, or indeed to any breach of contract, is a matter of construction of the contract. Many difficult questions arise and will continue to arise in the infinitely varied situations in which contracts come to be breached—by repudiatory breaches, accepted or not, by anticipatory breaches, by breaches of conditions or of various terms and whether by negligent, or deliberate action or otherwise. But there are ample resources in the normal rules of contract law for dealing with these without the superimposition of a judicially invented rule of law. I am content to leave the matter there with some supplementary observations.

1. The doctrine of ‘fundamental breach’ in spite of its imperfections and doubtful parentage has served a useful purpose. There was a large number of problems, productive of injustice, in which it was worse than unsatisfactory to leave exception clauses to operate. Lord Reid referred to these in the Suisse Atlantique case [1967] 1 AC 361, 406, pointing out at the same time that the doctrine of fundamental breach was a dubious specific. But since then Parliament has taken a hand: it has passed the Unfair Contract Terms Act 1977. This Act applies to consumer contracts and those based on standard terms and enables exception clauses to be applied with regard to what is just and reasonable. It is significant that Parliament refrained from legislating over the whole field of contract. After this Act, in commercial matters generally, when the parties are not of unequal bargaining power, and when risks are normally borne by insurance, not only is the case for judicial intervention undemonstrated, but there is everything to be said, and this seems to have been Parliament’s intention, for leaving the parties free to apportion the risks as they think fit and for respecting their decisions.
At the stage of negotiation as to the consequences of a breach, there is everything to be said for allowing the parties to estimate their respective claims according to the contractual provisions they have themselves made, rather than for facing them with a legal complex so uncertain as the doctrine of fundamental breach must be. What, for example, would have been the position of the respondents’ factory if instead of being destroyed it had been damaged, slightly or moderately or severely? At what point does the doctrine (with what logical justification I have not understood) decide, ex post facto, that the breach was (factually) fundamental before going on to ask whether legally it is to be regarded as fundamental? How is the date of ‘termination’ to be fixed? Is it the date of the incident causing the damage, or the date of the innocent party’s election, or some other date? All these difficulties arise from the doctrine and are left unsolved by it.

At the judicial stage there is still more to be said for leaving cases to be decided straightforwardly on what the parties have bargained for rather than upon analysis, which becomes progressively more refined, of decisions in other cases leading to inevitable appeals. The learned judge was able to decide this case on normal principles of contractual law with minimal citation of authority. I am sure that most commercial judges have wished to be able to do the same ... In my opinion they can and should.

2... . I have ... been unable to understand how the doctrine can be reconciled with the well accepted principle of law, stated by the highest modern authority, that when in the context of a breach of contract one speaks of ‘termination,’ what is meant is no more than that the innocent party or, in some cases, both parties, are excused from further performance. Damages, in such cases, are then claimed under the contract, so what reason in principle can there be for disregarding what the contract itself says about damages—whether it ‘liquidates’ them, or limits them, or excludes them? These difficulties arise in part from uncertain or inconsistent terminology. A vast number of expressions are used to describe situations where a breach has been committed by one party of such a character as to entitle the other party to refuse further performance: discharge, rescission, termination, the contract is at an end, or dead, or displaced; clauses cannot survive, or simply go. I have come to think that some of these difficulties can be avoided; in particular the use of ‘rescission,’ even if distinguished from rescission ab initio, as an equivalent for discharge, though justifiable in some contexts (see Johnson v Agnew [1980] AC 367) may lead to confusion in others. To plead for complete uniformity may be to cry for the moon. But what can and ought to be avoided is to make use of these confusions in order to produce a concealed and unreasoned legal innovation: to pass, for example, from saying that a party, victim of a breach of contract, is entitled to refuse
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further performance, to saying that he may treat the contract as at
an end, or as rescinded, and to draw from this the proposition,
which is not analytical but one of policy, that all or (arbitrarily)
some of the clauses of the contract lose, automatically, their force,
regardless of intention …

In this situation the present case has to be decided. As a
preliminary, the nature of the contract has to be understood.
Securicor undertook to provide a service of periodical visits for a
very modest charge which works out at 26p per visit. It did not
agree to provide equipment. It would have no knowledge of the
value of the plaintiffs’ factory; that, and the efficacy of their fire
precautions, would be known to the respondents. In these
circumstances nobody could consider it unreasonable, that as
between these two equal parties the risk assumed by Securicor
should be a modest one, and that the respondents should carry the
substantial risk of damage or destruction.

The duty of Securicor was, as stated, to provide a service. There
must be implied an obligation to use due care in selecting their
patrolmen, to take care of the keys and, I would think, to operate
the service with due and proper regard to the safety and security of
the premises. The breach of duty committed by Securicor lay in a
failure to discharge this latter obligation. Alternatively it could be
put upon a vicarious responsibility for the wrongful act of Musgrove
—viz., starting a fire on the premises: Securicor would be
responsible for this upon the principle stated in Morris v C.W.
Martin & Sons Ltd [1966] 1 QB 716, 739. This being the breach,
does condition 1 apply? It is drafted in strong terms, ‘Under no
circumstances’ … ‘any injurious act or default by any employee.’
These words have to be approached with the aid of the cardinal
rules of construction that they must be read contra proferentem
and that in order to escape from the consequences of one’s own
wrongdoing, or that of one’s servant, clear words are necessary. I
think that these words are clear. The respondents in facts [sic]
relied upon them for an argument that since they exempted from
negligence they must be taken as not exempting from the
consequence of deliberate acts. But this is a perversion of the rule
that if a clause can cover something other than negligence, it will
not be applied to negligence. Whether, in addition to negligence, it
covers other, e.g., deliberate, acts, remains a matter of construction
requiring, of course, clear words. I am of opinion that it does, and
being free to construe and apply the clause, I must hold that
liability is excluded …
7. Exemption clauses and unfair contract terms

1. Following a general construction test, it is unnecessary to distinguish a fundamental breach. It appears that the only relevance of a fundamental breach is that clearer words will be required for the clause to cover it.

2. However, in *Astrazeneca UK Ltd v Albermarle International Corporation* [2011] EWHC 1574 (Comm), [2011] 2 CLC 252, [2012] Bus LR D1, speaking *obiter*, Flaux J rejected the approach that had earlier been taken by the judge in *Internet Broadcasting Corporation Ltd (t/a NETTV) v Mar LLC (t/a MARHedge)* [2009] EWHC 844 (Ch), [2010] 1 All ER (Comm) 112, [2009] 2 Lloyd’s Rep 295, as ‘heterodox and regressive’. The judge in *MARHedge* had stated that there was a strong presumption against an exemption clause being construed to cover a deliberate repudiatory breach. Flaux J considered that this risked a return to the doctrine of fundamental breach that had been rejected in *Suisse Atlantique* and in the *Photo Production* case. Instead, the correct test ‘was one of construing the clause, albeit strictly, but without any presumption’. The clause in *Astrazeneca* provided that ‘[n]o claims by [AZ] of any kind, whether as to the products delivered or for non-delivery of the products’ would be permitted. The judge considered that this was ‘sufficiently clearly worded to cover any breach of the delivery obligations, deliberate or otherwise’.

3. In *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361, [2009] 1 All ER (Comm) 586, the Court of Appeal rejected an argument that the words ‘in any circumstances’ were wide enough to exclude recovery of losses for fraudulent or malicious damage.

4. In *Photo Production* the House of Lords also explicitly rejected the previous misconception that the effect of termination for fundamental breach was to bring the contract to an end so that the contractual terms no longer applied. On the contrary, although future performance is no longer required, the contract is *not* treated as being void *ab initio*. The terms are still relevant, e.g. for the purposes of assessing the measure of damages, and any exemption clause is still relevant for the purposes of assessing if liability has been excluded or limited.

5. The House of Lords in *Photo Production* seems to have been greatly influenced by the fact that the parties were ‘of equal bargaining power’, and so must be taken to have allocated the risk and, consequently, the burden of securing insurance cover. The other relevant factor was that the House viewed the cost of the service provided by Securicor as being very modest.
Is it true to say that the parties were of equal bargaining power when the claimants contracted on the defendants’ standard terms?

George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd

[1983] 2 AC 803 (HL)

The claimants purchased 30 lbs of Finney’s Late Dutch special cabbage seed, at a price of £201.60, from the defendant seed merchants with whom they had contracted for many years. The conditions of sale on the back of the invoice limited liability to replacement of the goods or a refund of the purchase price. The seed supplied was not late cabbage seed, but autumn cabbage seed of inferior variety. The claimants had planted the seed in 63 acres, but it did not grow into cabbage plants and had to be ploughed in. The claimants’ loss was more than £61,000. They claimed damages. Parker J, at first instance, held that since what was delivered was wholly different in kind from what had been ordered and agreed to be supplied, there was a fundamental breach and the clause could not operate. The majority of the Court of Appeal (Oliver and Kerr LJJ)—[1983] 1 QB 284—agreed, although they also found that the clause was unenforceable by virtue of the Sale of Goods Act 1979, s. 55, since it was not ‘fair and reasonable’ to allow reliance on it.

(p. 305) Held: The House of Lords agreed with Lord Denning MR, in the minority in the Court of Appeal, that the task of the judge was to give the clause its natural meaning and that, on their true construction, the conditions did cover the loss that had occurred. However, the House agreed with the Court of Appeal that it would not be ‘fair and reasonable’ to allow reliance on them. (On the question of the reasonableness of the clause, see page 320, section 7.4.5.1.)

LORD BRIDGE: My Lords, it seems to me, with all due deference, that the judgments of the learned trial judge and of Oliver LJ on the common law issue come dangerously near to re-introducing by the back door the doctrine of ‘fundamental breach’ which this House in Securicor 1 [Photo Production] [1980] AC 827, had so forcibly evicted by the front. The learned judge discusses what I may call the ‘peas and beans’ or ‘chalk and cheese’ cases, sc. those in which it has been held that exemption clauses do not apply where there has been a
contract to sell one thing, e.g. a motor car, and the seller has supplied quite another thing, e.g. a bicycle ...

In my opinion, this is not a ‘peas and beans’ case at all. The relevant condition applies to ‘seeds’ ... The relevant condition, read as a whole, unambiguously limits the appellants’ liability to replacement of the seeds or refund of the price. It is only possible to read an ambiguity into it by the process of strained construction which was deprecated by Lord Diplock [1980] AC 827, 851C in Securicor 1 and by Lord Wilberforce in Securicor 2 [Ailsa Craig] [1983] 1 WLR 964, 966G.

In holding that the relevant condition was ineffective to limit the appellants’ liability for a breach of contract caused by their negligence, Kerr LJ applied the principles stated by Lord Morton of Henryton giving the judgment of the Privy Council in Canada Steamship Lines Ltd v The King [1952] AC 192, 208. The learned Lord Justice stated correctly that this case was also referred to by Lord Fraser of Tullybelton in Securicor 2 [1983] 1 WLR 964, 970. He omitted, however, to notice that ... the whole point of Lord Fraser’s reference was to express his opinion that the very strict principles laid down in the Canada Steamship Lines case as applicable to exclusion and indemnity clauses cannot be applied in their full rigour to limitation clauses. Lord Wilberforce’s speech contains a passage to the like effect, and Lord Elwyn-Jones, Lord Salmon and Lord Lowry agreed with both speeches. Having once reached a conclusion in the instant case that the relevant condition unambiguously limited the appellants’ liability, I know of no principle of construction which can properly be applied to confine the effect of the limitation to breaches of contract arising without negligence on the part of the appellants. In agreement with Lord Denning MR, I would decide the common law issue in the appellants’ favour.

Notes

2. It is clear that any argument based upon the ‘peas and beans’ cases is unlikely to succeed in future as a method of preventing reliance on an exemption clause, since, given that there are to be no strained constructions, a court may not construe what has been delivered as being wholly different from what was ordered. The House of Lords construed this contract as a contract to deliver seed and seed had been delivered.
7. Exemption clauses and unfair contract terms

7.4 Clause in a B2B contract must not be rendered unenforceable by the Unfair Contract Terms Act 1977

7.4.1 Scope of UCTA 1977

UCTA 1977 places statutory restrictions on the extent to which liability or remedies can be ‘excluded or restricted’ by means of exemption clauses in B2B (business to business) contracts. Since UCTA 1977 broadly reflects a policy of non-intervention in such B2B cases, the scope of application of the Act is reduced now that, following the CRA 2015, it no longer applies to B2C (trader to consumer) contracts.

7.4.1.1 Section 13(1)

Section 13(1) of UCTA 1977 extends the definition of exemption clauses that may be regulated under the Act.

**Unfair Contract Terms Act 1977**

13. Varieties of exemption clause

(1) To the extent that this Part of this Act prevents the exclusion or restriction of any liability it also prevents—

(a) making the liability or its enforcement subject to restrictive or onerous conditions;

(b) excluding or restricting any right or remedy in respect of the liability, or subjecting a person to any prejudice in consequence of his pursuing any such right or remedy;

(c) excluding or restricting rules of evidence or procedure;

and (to that extent) sections 2, 6 and 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.

7.4.1.1.1 ‘No set-off’ clauses

Stewart Gill Ltd v Horatio Myer & Co. Ltd

[1992] 1 QB 600 (CA)

The claimants were to supply the defendants with an overhead conveyor system. Payment was in stages, with the final 10 per cent payable in the form of 5 per cent on completion and 5 per cent 30 days thereafter. The claimants’ general conditions of sale provided...
that the defendants could not withhold payment of any amount due on
grounds of set-off or counterclaim in respect of incorrect or defective
goods. The defendants withheld the final 10 per cent. They argued
that the claimants had committed various breaches of contract and
that these losses could be set off against the amount claimed.

**Held:** The clause prohibiting set-off was unenforceable. Section 13(1)
(b) extended the meaning of ss. 3 and 7 to cover this clause, since it
excluded a right that would otherwise be available. Therefore the
clause had to be shown to be reasonable. A term preventing an
overpayment being set off against a claim for the price was prima
facie unreasonable and, since the offending parts could not be
severed, the whole clause was unenforceable.

LORD DONALDSON MR: Section 3 of the 1977 Act applies
where, as here, one party to a contract deals with the other on
that other’s written standard terms of business. However, it is
limited to terms excluding or restricting liability or entitling the
party concerned to render no contractual performance or a
performance which is substantially different from that which
was reasonably expected of him. Clause 12.4 is not such a
clause, but the section is relevant to a consideration of section
13, although it is not there referred to in express terms. (p. 307)

Section 7 applies where, as here, the contract transfers the
ownership of goods otherwise than under a contract for the sale
or hire-purchase of goods. Unlike section 3, it is referred to in
section 13 but, like section 3, it is concerned with exclusion or
restriction of liability.

[Lord Donaldson then referred to section 13:]  

It is a trite fact (as contrasted with being trite law) that there
are more ways than one of killing a cat. Section 13 addresses
this problem. On behalf of the plaintiffs it was submitted that it
only did so to the extent of rendering ineffective any
unreasonable term which by for example introducing restrictive
or onerous conditions, indirectly achieved the exclusion or
restriction of liability which, if achieved directly, would fall
within the scope of other sections. The plaintiffs rightly say that
clause 12.4 does not have this effect. On behalf of the
defendants it was submitted that it had a wider scope.

The answer is, of course, to be found in the wording of the
section, but it does not exactly leap out of the print and hit one
between the eyes. Analysing the section and disregarding
words which are irrelevant, it seems to deal with the matter as
follows: ‘To the extent that this Part of this Act prevents the
exclusion or restriction of any liability it also prevents …’ This
seems to me to do no more than give expression to the ‘cat’ approach. Both sections 3 and 7 would render ineffective any clause in the plaintiffs’ written standard terms of business which excluded or restricted liability in respects which are here material and section 13 extends this in some way. In order to find out in what way, one must read on:

it also prevents—(a) making the liability or its enforcement subject to restrictive or onerous conditions; (b) excluding or restricting any right or remedy in respect of the liability ... (c) excluding or restricting rules of ... procedure ...

Now clause 12.4 can perhaps be said to make the enforcement of the plaintiffs’ liability subject to a condition that the defendants shall not have sought to set off their own claims against their liability to pay the price and this might well be said to be onerous. However, I do not think it necessary to pursue this, because it is quite clear that clause 12.4 excludes the defendants’ ‘right’ to set off their claims against the plaintiffs’ claim for the price and further excludes the remedy which they would otherwise have of being able to enforce their claims against the plaintiffs by means of a set-off: see paragraph (b). It also excludes or restricts the procedural rules as to set off: see paragraph (c). Thus far, therefore, the defendants can bring themselves within the section.

We then get to the words:

and (to that extent) sections 2 and 5 to 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.

Although I find this obscure, I do not think that these words restrict the ambit of the preceding words. I think that they constitute an extension and that what is intended to be covered is an exclusion or restriction of liability not by contract but by reference to notices or terms of business which are not incorporated in a contract. If this is correct, it is irrelevant to the present case.
7. Exemption clauses and unfair contract terms

Section 13(1) provides that clauses are subject to ss. 2, 6, or 7 of UCTA 1977 if they are worded as clauses that exclude or restrict the obligation or duty.

[1990] 1 AC 831 (HL)
A prospective purchaser applied for a mortgage and the building society instructed the defendants to value the property. The applicant signed a form containing a disclaimer, which stated that neither the building society nor its surveyor warranted that the report and valuation would be accurate, and that the report and valuation were supplied without any acceptance of responsibility. The report also contained a similar disclaimer. The valuation stated that no essential repairs were required. It was negligently prepared and the purchaser claimed damages in tort from the defendants. The defendants argued that the disclaimer was effective to protect them and was not subject to UCTA 1977, s. 2(2) (see page 313, section 7.4.3), because it was not a clause that excluded liability.

Held: A duty of care was owed by the valuers to the prospective purchaser. The disclaimer was subject to UCTA 1977, s. 2, in that the last part of s. 13(1) stated that s. 2 applied to clauses that purported to prevent the duty ever arising.

LORD TEMPLEMAN: In Harris v Wyre Forest DC [1988] QB 835 the Court of Appeal ... accepted an argument that the 1977 Act did not apply because the council by their express disclaimer refused to obtain a valuation save on terms that the valuer would not be under any obligation to Mr and Mrs Harris to take reasonable care or exercise reasonable skill. The council did not exclude liability for negligence but excluded negligence so that the valuer and the council never came under a duty of care to Mr and Mrs Harris and could not be guilty of negligence. This construction would not give effect to the manifest intention of the Act but would emasculate the Act. The construction would provide no control over standard form exclusion clauses which

Notes

1. Compare this decision with Schenkers Ltd v Overland Shoes Ltd [1998] 1 Lloyd’s Rep 498 (see page 325, section 7.4.5.2).
2. Since s. 5 UCTA 1977 was repealed by the CRA 2015, the final words of s. 13 now apply only to ss. 2, 6, and 7 UCTA 1977.
individual members of the public are obliged to accept. A party to a contract or a tortfeasor could opt out of the Act of 1977 by declining in the words of Nourse LJ, at p. 845, to recognise ‘their own answerability to the plaintiff’. Caulfield J said, at p. 850, that the Act ‘can only be relevant where there is on the facts a potential liability’. But no one intends to commit a tort and therefore any notice which excludes liability is a notice which excludes a potential liability. Kerr LJ, at p. 853, sought to confine the Act to ‘situations where the existence of a duty of care is not open to doubt’ or where there is ‘an inescapable duty of care’. I can find nothing in the Act of 1977 or in the general law to identify or support this distinction. In the result the Court of Appeal held that the Act does not apply to ‘negligent misstatements where a disclaimer has prevented a duty of care from coming into existence’; per Nourse LJ, at p. 848. My Lords, this confuses the valuer’s report with the work which the valuer carries out in order to make his report. The valuer owed a duty to exercise reasonable skill and care in his inspection and valuation. If he had been careful in his work, he would not have made a ‘negligent misstatement’ in his report.

... Section 13(1) of the Act prevents the exclusion of any right or remedy and (to that extent) section 2 also prevents the exclusion of liability: ‘by reference to ... notices which exclude ... the relevant obligation or duty.’

...

The answer to the second question involved in these appeals is that the disclaimer of liability made by the council on its own behalf in the *Harris* case and by the Abbey National on behalf of the appellant surveyors in the *Smith* case constitute notices which fall within the Unfair Contract Terms Act 1977 and must satisfy the requirement of reasonableness.

### NOTE

This scenario would now fall within Part 2 of the CRA 2015. However, it provides useful continuing authority for the fact that a disclaimer of duty or responsibility in a B2B contract can be subjected to UCTA 1977 regulation as falling within the definition of an exemption clause.
Thompson v T. Lohan (Plant Hire) Ltd & J. W. Hurdiss Ltd

[1987] 1 WLR 649 (CA)

The defendants, a plant hire company, hired an excavator and driver to Hurdiss for use by Hurdiss at its quarry. The hire was on the terms and conditions of the Contractors’ Plant Association, clause 8 of which provided:

When a driver or operator is supplied by the owner with the plant, the owner shall supply a person competent in operating the plant and such person shall be under the direction and control of the hirer. Such drivers or operators shall for all purposes in connection with their employment in the working of the plant be regarded as the servants or agents of the hirer ... who alone shall be responsible for all claims arising in connection with the operation of the plant by the said drivers or operators. The hirer shall not allow any other person to operate such plant without the owner’s previous consent to be confirmed in writing.

Clause 13 provided that the hirer was to ‘fully and completely indemnify the owner in respect of all claims by any person whatsoever for injury to person or property caused by or in connection with or arising out of the use of the plant’. The claimant’s husband was killed in an accident caused by the negligence of the driver in operating the excavator at the quarry. The claimant succeeded in her claim for damages in tort from the defendants, and the defendants sought to rely on clauses 8 and 13 to recover the damages from Hurdiss. Hurdiss argued, inter alia, that the conditions were contrary to s. 2(1) of UCTA 1977 (see page 313, section 7.4.3) and could not be relied upon.

Held: Clause 8 transferred liability for the driver’s negligence to the third party, Hurdiss, who therefore had to indemnify the defendants under clause 13. Section 2 of the 1977 Act was intended to prevent the exclusion of liability in negligence to the victim of the negligence (the claimant) and was not concerned with arrangements, such as those made in clause 8, for sharing or transferring the burden of compensating the victim. It therefore had no application on the facts.

The Court of Appeal distinguished Phillips Products Ltd v Hyland [1987] 1 WLR 659. In Phillips, the claimants hired an excavator and a driver from the defendants to carry out building work at the
claimants’ factory. The contract of hire incorporated clause 8 of the Contractors’ Plant Association conditions. The driver negligently drove the excavator into a wall and caused considerable damage to the claimants’ property. The claimants claimed damages from the defendants, who sought to rely on clause 8. The claimants alleged that clause 8 was subject to s. 2(2) of UCTA 1977, since it purported to ‘exclude or restrict’ liability in negligence. The Court of Appeal agreed. The court considered that, in deciding whether a clause had excluded or restricted liability, the court had to look at the substance and effect of the term rather than its form. In the circumstances, the effect of clause 8 was to negative the common law duty in tort, which otherwise would have been owed by the defendants. Therefore clause 8 had the effect of excluding liability and fell within s. 2(2) of the 1977 Act.

The position was very different on the facts in Thompson, as Fox LJ explained.

(p. 310)

FOX LJ: In the Phillips case there was a tortfeasor, Hamstead, who were vicariously liable to Phillips for the damage done by their servant, Hyland. Thus Hamstead were liable to Phillips for negligence, but were seeking to exclude that liability by relying on clause 8. If that reliance had been successful, the result in the Phillips case would be that the victim would be left with no remedy by virtue of the operation of clause 8. Prima facie the victim was entitled to damages for negligence against Hamstead, because Hamstead were vicariously liable in negligence for the acts of their own servant. So one starts from that point. There was a plain liability of Hamstead to Phillips. That was, as Slade LJ said, a case of a plant owner excluding his liability for negligence in the relevant sense by reference to the contract term, clause 8 ...

If one then turns to the present case, the sharp distinction between it and the Phillips case is this, that whereas in the Phillips case there was a liability in negligence of Hamstead to Phillips (and that was sought to be excluded), in the present case there is no exclusion or restriction of the liability sought to be achieved by reliance upon the provisions of clause 8. The plaintiff has her judgment against Lohan and can enforce it. The plaintiff is not prejudiced in any way by the operation sought to be established of clause 8. All that has happened is that Lohan and the third party have agreed between themselves who is to bear the consequences of Mr Hill’s negligent acts. I can see nothing in section 2(1) of the Act of 1977 to prevent that. In my opinion, section 2(1) is concerned with protecting the victim of negligence, and of course those who claim under
7. Exemption clauses and unfair contract terms

him. It is not concerned with arrangements made by the wrongdoer with other persons as to the sharing or bearing of the burden of compensating the victim. In such a case it seems to me there is no exclusion or restriction of the liability at all. The liability has been established by Hodgson J. It is not in dispute and is now unalterable. The circumstance that the defendants have between themselves chosen to bear the liability in a particular way does not affect that liability; it does not exclude it, and it does not restrict it. The liability to the plaintiff is the only relevant liability in the case, as it seems to me, and that liability is still in existence and will continue until discharge by payment to the plaintiff. Nothing is excluded in relation to the liability, and the liability is not restricted in any way whatever. The liability of Lohan to the plaintiff remains intact. The liability of Hamstead to Phillips was sought to be excluded.

NOTE

The loss in Phillips Products v Hyland was incurred by the hirer, so that the clause could easily be seen as excluding liability, whereas in Thompson it was the loss of a third party. They are consistent in that in both it is the position of the victim that is important.

7.4.1.3 Evasion by means of secondary contract

Unfair Contract Terms Act 1977

10. Evasion by means of secondary contract

A person is not bound by any contract term prejudicing or taking away rights of his which arise under; or in connection with the performance of, another contract, so far as those rights extend to the enforcement of another’s liability which this Part of this Act prevents that other from excluding or restricting.

Tudor Grange Holdings Ltd v Citibank NA
Tudor Grange brought an action against Citibank. Citibank sought to have it struck out on the ground that Tudor Grange had agreed a deed of release that prevented the action. This deed of release released the bank from ‘all claims, demands and causes of action whether or not presently known or suspected’, but Tudor Grange claimed that it was unenforceable under s. 10 of UCTA 1977. The company argued that the release took away its rights under the banking contract with Citibank, including its right to complain of breaches of the duty of care owed in the banking contract, which the bank was precluded by UCTA 1977 from excluding or restricting unless the release was shown to be reasonable.

Held: Section 10 did not apply to a contract to settle disputes that had arisen concerning the performance of an earlier contract. In addition, it could not apply where the parties to both contracts were the same. The release was therefore binding on Tudor Grange.

BROWNE-WILKINSON V-C: This argument that s. 10 of the Act may apply to compromises or settlement of existing disputes has been foreseen by a number of textbook writers as an unfortunate possibility. They are unanimous in their hope that the courts will be robust in resisting it. If [counsel for the plaintiffs’] construction is correct, the impact will be very considerable. The Act of 1977 is normally regarded as being aimed at exemption clauses in the strict sense, that is to say, clauses in a contract which aim to cut down prospective liability arising in the course of the performance of the contract in which the exemption clause is contained. If [counsel for the plaintiffs’] argument is correct, the Act will apply to all compromises or waivers of existing claims arising from past actions. Any subsequent agreement to compromise contractual disputes falling within sections 2 or 3 of the Act will itself be capable of being put in question on the grounds that the compromise or waiver is not reasonable. Even an action settled at the door of the court on the advice of solicitors and counsel could be reopened on the grounds that the settlement was not reasonable within the meaning of the Act. If I am forced to that conclusion by the words of section 10 properly construed, so be it. But, in my judgment, it is improbable that Parliament intended that result: it would be an end to finality in seeking to resolve disputes.

The starting point in construing section 10 is, in my judgment, to determine the mischief aimed at by the Act itself. For this purpose, it is legitimate to look at the second report on exemption clauses of the Law Commission on Exemption Clauses (1975) (Law Com No. 69): (see Smith v Eric S Bush
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[1990] AC 831, 857E, per Lord Griffiths). This report was the genesis of the Act of 1977. The report is wholly concerned with remedying injustices which are caused by exemption clauses in the strict sense. So far as I can see, the report makes no reference of any kind to any mischief relating to agreements to settle disputes.

Next, the marginal note to section 10 reads: ‘Evasion by means of secondary contract.’ ... This sidenote clearly indicates that it is aimed at devices intended to evade the provisions of Pt 1 of the Act of 1977 by the use of another contract. In my judgment, a contract to settle disputes which have arisen concerning the performance of an earlier contract cannot be described as an evasion of the provisions in the Act regulating exemption clauses in the earlier contract. Nor is the compromise contract ‘secondary’ to the earlier contract.

The textbooks, to my mind correctly, identify at least one case which section 10 is designed to cover. Under contract 1, the supplier (S) contracts to supply a customer (C) with a product. Contract 1 contains no exemption clause. However, C enters into a servicing contract, contract 2, with another party (X). Under contract 2, C is precluded from exercising certain of his rights against S under contract 1. In such a case section 10 operates to preclude X from enforcing contract 2 against C so as to prevent C enforcing his rights against S under contract 1. The extent of the operation of section 10 in such circumstances may be doubtful: see Treitel on The Law of Contract, 7th edn, (1987), p. 206. But there is no doubt that such a case falls squarely within the terms of section 10.

In the case that I have just postulated, the references in section 10 to ‘another’s liability’ and ‘that other’ are references to someone other than X, i.e. to the original supplier, S. On [counsel for the plain tiffs’] construction the words ‘another’ and ‘that other’ are taken as referring to someone other than C, the customer whose rights are restricted, so as to make the section apply to a case such as the present where there is no third party, X. Although as a matter of language the words of the section are capable of referring to anyone other than C, in my judgment, read in context and having regard to the purpose both of the Act and of the section itself, the reference to ‘another’ plainly means someone other than X, that is to say someone other than the party to the secondary contract. In my judgment, section 10 does not apply where the parties to both contracts are the same.
This view is reinforced by a further factor. If the Act were intended to apply to terms in subsequent compromise agreements between the same parties as the original contract, section 10 would be quite unnecessary. Under sections 2 and 3 there is no express requirement that the contract term excluding or restricting S’s liability to C has to be contained in the same contract as that giving rise to S’s liability to C. If S and C enter into two contracts, it makes no difference if the exemption clause is contained in a different contract from that under which the goods are supplied. Sections 2 and 3 by themselves will impose the test of reasonableness. Why then should Parliament have thought that in section 10 there was some possibility of evasion in such circumstances?

In my judgment, the Act of 1977 is dealing solely with exemption clauses in the strict sense (i.e. clauses in a contract modifying prospective liability) and does not affect retrospective compromises of existing claims. Section 10 is dealing only with attempts to evade the Act’s provisions by the introduction of such an exemption clause into a contract with a third party … Accordingly, for those reasons, section 10 cannot apply to the release ...

NOTE

Section 10 is limited to attempts to avoid the operation of the provisions of UCTA 1977 by the use of an exemption clause in a secondary contract with a third party.

By comparison, s. 72 CRA 2015 contains a provision addressing so-called ‘evasion by secondary contract’ in the B2C context, and whereas this provision is clear that it does not apply to bring the secondary contract clause in question within Part 2 CRA 2015 if it is a settlement agreement in relation to the main contract liabilities, it will apply to other secondary contracts—whether between the parties to the main contract or with a third party.

7.4.1.4 Business liability

The main provisions of the 1977 Act (ss. 2–7) apply only to ‘business liability’.
7. Exemption clauses and unfair contract terms

Unfair Contract Terms Act 1977

1. Scope of Part I

(3) In the case of both contract and tort, sections 2 to 7 apply (except where the contrary is stated in section 6(4)) only to business liability, that is liability for breach of obligations or duties arising—

(a) from things done or to be done by a person in the course of a business (whether his own business or another’s); or

(b) from the occupation of premises used for business purposes of the occupier; and references to liability are to be read accordingly but liability of an occupier of premises for breach of an obligation or duty towards a person obtaining access to the premises for recreational or educational purposes, being liability for loss or damage suffered by reason of the dangerous state of the premises, is not a business liability of the occupier unless granting that person such access for the purposes concerned falls within the business purposes of the occupier.

7.4.2 Basic scheme of UCTA 1977

UCTA 1977 deals with exemption clauses as follows: either the clause is rendered totally unenforceable in the circumstances; or the clause is unenforceable unless it is established that it is reasonable (thus not every clause is subject to the reasonableness requirement).

The first step is to find the section applicable to the liability sought to be excluded. This will then tell us whether the clause is totally unenforceable or subject to the reasonableness requirement.
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7.4.3 Negligence liability (s. 2)

Unfair Contract Terms Act 1977

1. Scope of Part I

For the purposes of this Part of this Act, ‘negligence’ means the breach—

(a) of any obligation, arising from the express or implied terms of a contract, to take reasonable care or exercise reasonable skill in the performance of the contract;
(b) of any common law duty to take reasonable care or exercise reasonable skill (but not any stricter duty);
(c) of the common duty of care imposed by the Occupiers’ Liability Act 1957 or the Occupiers’ Liability Act (Northern Ireland) 1957.

For the purposes of the Act, certain breaches of contract are treated as negligence (i.e. breaches of qualified contractual obligations to take reasonable care or to exercise reasonable skill).

Unfair Contract Terms Act 1977

2. Negligence liability

(1) A person cannot by reference to any contract term or to a notice given to persons generally or to particular persons exclude or restrict his liability for death or personal injury resulting from negligence.
(2) In the case of other loss or damage, a person cannot so exclude or restrict his liability for negligence except in so far as the term or notice satisfies the requirement of reasonableness.

NOTE

Clauses that purport to exclude or restrict negligence liability for death or personal injury are rendered totally unenforceable. ‘Other loss or damage’ means loss or damage other than death or personal injury, and would include property damage and economic loss. Clauses falling within s. 2(2) are enforceable only if shown to be reasonable. When a clause aims to exclude liability for death or personal injury as well as other grounds, Goodlife Foods Ltd v Hall
7. Exemption clauses and unfair contract terms

**Fire Protection Ltd** [2017] EWHC 767 (TCC), [2017] BLR 389 highlights that the part pertaining to excluding death and personal injury is severed. The clause is then assessed solely on the permitted exclusion.

Section 2 does not apply to consumer contracts (UCTA 1977, s. 2(4)), but s. 65 CRA 2015 is an equivalent provision.

7.4.4 Contractual liability

Contractual liability is dealt with in two places in the 1977 Act. Special rules in ss. 6–7 cover certain implied obligations (e.g. as to title, description, fitness for purpose, satisfactory quality, and correspondence with sample) in sale of goods and hire purchase contracts, contracts for work and materials, and hire contracts (for details of these contracts and terms, see page 269, Chapter 6, section 6.4.2). Secondly, a general provision covers contractual liability where one party deals on the other’s written standard terms of business (s. 3). If this is not the position, then s. 3 regulation cannot apply.

7.4.4.1 Contractual liability covered by ss. 6–7

**Unfair Contract Terms Act 1977**

6. Sale and hire purchase

_(1A) Liability for breach of the obligations arising from—
(a) section 13, 14 or 15 of the 1979 Act (seller’s implied undertakings as to conformity of goods with description or sample, or as to their quality or fitness for a particular purpose);
(b) section 9, 10 or 11 of the 1973 Act (the corresponding things in relation to hire purchase), cannot be excluded or restricted by reference to a contract term except in so far as the term satisfies the requirement of reasonableness._

Notes

1. Under s. 6(1) of UCTA 1977 the implied obligations as to title cannot be excluded or restricted. Under s. 7(3A) liability for breach of s. 2 of the Supply of Goods and Services Act 1982 (relating to the transfer of goods in a work and materials contract) cannot be excluded or restricted. However, liability for breach of s. 7 of the 1982 Act (implied obligation concerning the
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right to transfer possession of goods in a hire contract) can be excluded or restricted if the clause satisfies the reasonableness test (UCTA 1977, s. 7(4)).

2. Similarly, under ss. 6(1A) and 7(1A) liability for breach of these implied goods obligations can be excluded provided the clause is reasonable. Of note, s. 6(1A) applies to sale of goods and hire purchase contracts; s. 7(1A) applies to work and materials contracts or hire contracts.

7.4.4.2 Section 3 (general contractual liability)

Any clause that attempts to exclude or restrict liability for strict (absolute) obligations arising under a contract, other than those covered by ss. 6–7 of UCTA 1977, may be covered by s. 3, if it applies.

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**Unfair Contract Terms Act 1977**

3. Liability arising in contract

(1) This section applies as between contracting parties where one of them deals on the other’s written standard terms of business.

(2) As against that party, the other cannot by reference to any contract term—

(a) when himself in breach of contract, exclude or restrict any liability of his in respect of the breach; or

(b) claim to be entitled—

(i) to render a contractual performance substantially different from that which was reasonably expected of him, or

(ii) in respect of the whole or any part of his contractual obligation, to render no performance at all,

except in so far as (in any of the cases mentioned above in this subsection) the contract term satisfies the requirement of reasonableness.

(3) This section does not apply to a term in a consumer contract (but see the provision made about such contracts in section 62 of the Consumer Rights Act 2015).

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**NOTE**
7. Exemption clauses and unfair contract terms

Section 3, when applicable, is subject to the reasonableness requirement (see next paragraph). Two particular issues arise before that requirement can come into play. First, s. 3 does not apply to general contractual liability between two businesses unless one of the parties is dealing ‘on the other’s written standard terms of business’, as per s. 3(1). The expression is however not defined by the Act. Secondly, precisely what s. 3(2)(b) is meant to cover must also be assessed.

7.4.4.2.1 Dealing ‘on the other’s written standard terms’

Yuanda (UK) Co. Ltd v WW Gear Construction Ltd


EDWARDS-STUART J: 21 ... The conditions have to be standard in that they are terms which the company in question uses for all, or nearly all, of its contracts of a particular type without alteration (apart from blanks which have to be completed showing the price, name of the other contracting party and so on). One encounters such terms on a regular basis—whether when buying goods over the internet or by mail order or when buying a ticket for travel by air or rail.

22 In my view, it is the essence of such terms that they are not varied from transaction to transaction. If they were, they would no longer be ‘standard.’ However, there is a class of transactions where the standard terms are incorporated by reference as one part of a larger package of terms. For example, the standard terms so incorporated may relate only to delivery and acceptance of goods and have nothing to do with other aspects of the contract, such as the fitness for purpose of the goods or their suitability for a particular purpose. In such cases it is probably a matter of degree whether one contracting party is or is not dealing on its written standard terms ... 

24 [The defendant, Gear, seeking to deny the application of s.3 UCTA on the facts] ... relied on a decision of Judge Thayne Forbes QC in Salvage Association v CAP Financial Services Ltd [1995] FSR 654, in which he listed a number of facts that it might be appropriate to take into account when deciding
whether or not one party dealt with the other on the latter’s ‘written standard terms of business’. He said, at p 672:

The terms of the second contract were based on and closely followed CAP’s standard conditions of business and the use of those standard conditions as the starting point for negotiating and agreeing the precise terms of the second contract was an obvious and sensible way to approach the matter. In my opinion, the fact that a set of CAP’s standard conditions of business was used for this purpose does not necessarily mean that SA ‘dealt’ on CAP’s ‘written standard terms of business’. In such circumstances, whether it continues to be correct to describe the terms of the contract eventually agreed by the parties as the standard terms of business of the party who originally put them forward will be a question of fact and degree to be decided in all the circumstances of the particular case. Without attempting to give an exhaustive list of the type of facts which I think would be appropriate to take into account in arriving at such a decision, I consider that the following would be included: (i) the degree to which the ‘standard terms’ are considered by the other party as part of the process of agreeing the terms of the contract; (ii) the degree to which the ‘standard terms’ are imposed on the other party by the party putting them forward; (iii) the relative bargaining power of the parties; (iv) the degree to which the party putting forward the ‘standard terms’ is prepared to entertain negotiations with regard to the terms of the contract generally and the ‘standard terms’ in particular; (v) the extent and nature of any agreed alterations to the ‘standard terms’ made as a result of the negotiations between the parties; (vi) the extent and duration of the negotiations.

25 In St Albans City and District Council v International Computers Ltd [1996] 4 All ER 481, 490–491 Nourse LJ said:

... Did the plaintiffs ‘deal’ on the defendant’s written standard terms of business? [Counsel] submitted that the question must be answered in the negative, on the ground that you cannot be said to deal on another’s standard terms of business if, as was here the case, you negotiate with him over those terms before you enter into the contract. In my view that is an impossible construction for two reasons: first, because as a matter of plain English ‘deals’ means ‘makes a deal’, irrespective of
any negotiations that may have preceded it; secondly, because section 12(1)(a) equates the expression ‘deals as consumer’ with ‘makes the contract’. Thus it is clear that in order that one of the contracting parties may deal on the other’s written standard terms of business within section 3(1) it is only necessary for him to enter into the contract on those terms. [Counsel] sought to derive support for his submission from observations of Judge Thayne Forbes QC in Salvage Association v CAP Financial Services Ltd [1995] FSR 654, 671-672. In my view, those observations do not assist the defendant. In that case the judge had to consider, in relation to two contracts, whether certain terms satisfied the description ‘written standard terms of business’ and also whether there had been a ‘dealing’ on those terms. In relation to the first contract he said, at p 671: ‘I am satisfied that the terms in question were ones which had been written and produced in advance by CAP as a suitable set of contract terms for use in many of its future contracts of which the first contract with [the Salvage Association] happened to be one. It is true that Mr Jones felt free to and did negotiate and agree certain important matters and details relating to the first contract at the meeting of 27 February 1987. However, although he had read and briefly considered CAP’s conditions of business, he did not attempt any negotiation with regard to those conditions, nor did he or Mr Ellis consider that it was appropriate or necessary to do so. The CAP standard conditions were terms that he and Mr Ellis willingly accepted as incorporated into the first contract in their predetermined form. In those circumstances, it seems to me that those terms still satisfy the description ‘written standard terms of business’ and, so far as concerns the first contract, the actions of Mr Jones and Mr Ellis constituted ‘dealing’ on the part of [the Salvage Association] with CAP on its written standard terms of business within the meaning of section 3 of the [Unfair Contract Terms Act 1977].’ It is true that the judge found that the Salvage Association did not negotiate with CAP over the latter’s standard terms and that he held that, in entering into the contract, the Salvage Association dealt with CAP on those terms within section 3. I do not, however, read his observations as indicating a view that the ‘dealing’ depended on the absence of negotiations. I think that even if there had been negotiations over the standard conditions his view would have been the same. Scott Baker J dealt with this question as one of fact, finding that the defendant’s general conditions remained effectively untouched in the negotiations and that the plaintiffs accordingly dealt on
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the defendant’s written standard terms for the purposes of section 3(1): see [1995] FSR 686, 706. I respectfully agree with him.

26 I agree that factors (i), (ii) and (iv) of those identified in the Salvage Association case may be relevant in deciding whether or not a particular set of terms may constitute a party’s standard terms of business, at least when they are proffered, but I do not consider that the existence of negotiations is itself a relevant consideration: the St Albans case held that it was not. In my view, the only important factor of those listed in the Salvage Association case is (v). If there is any significant difference between the terms proffered (p. 317) and the terms of the contract actually made, then the contract will not have been made on one party’s written standard terms of business.

27 Whilst I would be prepared to accept in principle that some alterations to the proffered standard terms may be so insignificant as to make it possible to hold that the party has dealt on the others written standard terms of business (as was the case in Horace Holman Group Ltd v Sherwood International Group Ltd (unreported) 12 April 2000), I am quite satisfied that that is not the case here. The alterations negotiated by Yuanda were material, from a contractual point of view, and cannot be dismissed as de minimis.

28 In my judgment, therefore, this is plainly not a case where Yuanda dealt on Gear’s written standard terms of business. There are at least two reasons for this, both of which are fatal to Yuanda’s case. First, Yuanda itself negotiated some material alterations to the proffered ‘standard’ terms and this means that it did not deal on the ‘standard’ terms. As the decision in the St Albans case [1996] 4 All ER 481 makes clear, the reference to dealing in section 3 of the 1977 Act is to the making of the contract, not to its negotiation.

29 Second, the evidence shows that few, if any, of the 30-odd trade contractors entered into contracts which were on the same terms. Nearly all of them, during the pre-contract negotiations, appear to have secured alterations to the schedule of amendments originally put forward by Gear. This in itself shows that Gear did not have standard terms on which it dealt. The court is concerned with the terms on which the contract is actually made, not the terms that were proffered by one party to the other as the basis for the proposed contract. Whilst the latter may have been standard, so far as Gear was concerned, the former were not.
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For these reasons I conclude that Yuanda did not deal on Gear’s written standard terms of business for the purposes of section 3 of the 1977 Act.

Summary: Yuanda, and other first instance decisions dealing with the issue, were approved by the Court of Appeal in African Export-Import Bank v Shebah Exploration and Production Co Ltd [2017] EWCA Civ 845, [2018] 1 WLR 487. Summarizing the issues, Longmore LJ stated, at [18], that the most important elements are whether the term is part of the other party’s standard terms of business and whether the party is dealing on those written standard term of business. On the latter one and whether on the facts this is indeed the case, Longmore LJ specifically agreed with the regularity element highlighted by Edwards-Stuart J in Yuanda (at [21]). He therefore concluded at [25] that ‘it is relevant to inquire whether there have been more insubstantial variations to the terms which may have otherwise been habitually used by the other party to the transaction’ (emphasis added).

7.4.4.2.2 The meaning of s 3(2)(b)

Clauses covered by s. 3(2)(b) are those that define the obligation in a more limited way, so that a breach is less likely. This is necessary because the last part of s. 13 does not apply to s. 3 (see page 306, section 7.4.1.1).

Section 3(2)(b)(i) is seemingly designed to cover the possibility that the clause may allow the contractual performance to be altered in some way. In AXA Sun Life Services plc v Campbell Martin [2011] EWCA Civ 133, [2012] Bus LR 2013, [2011] 1 CLC 312, Stanley Burnton LJ noted that it was not clear how s. 3(2)(b)(i) should operate.

... Quite how that ‘paragraph’ should operate is not entirely clear, as is demonstrated by the somewhat tentative discussion in Chitty on Contracts, 30th ed (2008), vol 1, para 14-073. I have no doubt that it is principally aimed at the small print that entitles a party to a contract to provide something other than that defined by the principal terms of the contract, as where a holiday company reserves the right to substitute a hotel or resort for that specified in the main part of the contract. In most cases, as Chitty suggests, the performance reasonably expected of a party is that which is defined by the written contract between the parties. But this ‘paragraph’ of section 3 refers not to the performance specified in the contract but to the performance ‘which was reasonably expected’ of that party.

The issue will therefore be whether the clause is unreasonable in allowing changes to be made unilaterally from what had apparently been agreed.
under the main provisions of the contract and what was ‘reasonably expected’. However, this raises the question of how these reasonable expectations are to be established.

Once it is clear that s. 3 applies, the clause in question must satisfy the reasonableness requirement in s. 11 to be enforceable.

7.4.5 The reasonableness requirement

NOTE:

Apply this test only if the applicable section requires this, e.g. ss. 2(2), 3, 6(1A), and 7(1A).

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11. The ‘reasonableness’ test

(1) In relation to a contract term, the requirement of reasonableness for the purposes of this Part of this Act ... is that the term shall have been a fair and reasonable one to be included having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made.

(2) In determining for the purposes of section 6 or 7 above whether a contract term satisfies the requirement of reasonableness, regard shall be had in particular to the matters specified in Schedule 2 to this Act; but this subsection does not prevent the court or arbitrator from holding, in accordance with any rule of law, that a term which purports to exclude or restrict any relevant liability is not a term of the contract.

(3) In relation to a notice (not being a notice having contractual effect), the requirement of reasonableness under this Act is that it should be fair and reasonable to allow reliance on it, having regard to all the circumstances obtaining when the liability arose or (but for the notice) would have arisen.
7. Exemption clauses and unfair contract terms

(4) Where by reference to a contract term or notice a person seeks to restrict liability to a specified sum of money, and the question arises (under this or any other Act) whether the term or notice satisfies the requirement of reasonableness, regard shall be had in particular (but without prejudice to subsection (2) above in the case of contract terms) to—
(a) the resources which he could expect to be available to him for the purpose of meeting the liability should it arise; and
(b) how far it was open to him to cover himself by insurance.

(5) It is for those claiming that a contract term or notice satisfies the requirement of reasonableness to show that it does.

Notes

1. The reasonableness of the clause is to be judged at the time the contract was made. Some of the case law on reasonableness was actually decided on the basis of the test used in the Supply of Goods (Implied Terms) Act 1973 (Sale of Goods Act 1979, s. 55), i.e. whether it is fair and reasonable to allow reliance on the term. In these cases, reasonableness was judged after the breach had occurred. The Sale of Goods Act (SGA) 1979, s. 55 (set out in SGA 1979, Sch. 1, para. 11) applied to contracts made between the date on which the 1973 Act came into force and the date on which UCTA 1977 came into force.

2. What factors are relevant in determining reasonableness? Under section 11(4) two factors are particularly relevant to reasonableness. The availability and cost of insurance is one of these factors, but it has been used more generally by the courts: see e.g. Photo Production Ltd v Securicor Transport Ltd [1980] AC 827 and again in Goodlife Foods Ltd v Hall Fire Protection Ltd [2018] EWCA Civ 1371.

3. Section 11(2) refers to guidelines in Sch. 2, which are stated to be relevant to reasonableness in ss. 6 and 7. Owing to their factual relevancy, however, they have been used more widely: see Stuart Smith LJ in Stewart Gill Ltd v Horatio Myer & Co. Ltd [1992] 1 QB 600, 608.
Unfair Contract Terms Act 1977

Schedule 2 ‘Guidelines’ for application of reasonableness test

The matters to which regard is to be had in particular for the purposes of sections 6(1A), 7(1A) and

(4) … are any of the following which appear to be relevant—

(a) the strength of the bargaining positions of the parties relative to each other, taking into account (among other things) alternative means by which the customer’s requirements could have been met;
(b) whether the customer received an inducement to agree to the term, or in accepting it had an opportunity of entering into a similar contract with other persons, but without having to accept a similar term;
(c) whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any previous course of dealing between the parties);
(d) where the term excludes or restricts any relevant liability if some condition is not complied with, whether it was reasonable at the time of the contract to expect that compliance with that condition would be practicable;
(e) whether the goods were manufactured, processed or adapted to the special order of the customer.

Notes

1. The most fundamental factor in practice has been the question of the parties’ bargaining positions. It is clearly more reasonable to use such a clause where the parties’ bargaining position is equal.
2. As regards condition (c), the Court of Appeal in AEG (UK) Ltd v Logic Resource Ltd [1996] CLC 265 (see page 238, Chapter 6, section 6.3.1.4) made it clear that the fact that a clause had been incorporated as a term did not necessarily mean that the clause would satisfy the reasonableness test. Schedule 2(c) requires an examination of the reality of the consent to the term. It presupposes that the term has already been incorporated as a term of the contract, but assesses the extent to which the party has actually consented to it.
7. Exemption clauses and unfair contract terms

3. The presentation of the clause can be significant when assessing its reasonableness. In *Stag Line Ltd v Tyne Ship Repair Group Ltd, The Zinnia* [1984] 2 Lloyd’s Rep 211, the most important factor affecting reasonableness was that the parties were of equal bargaining power, but Staughton J stated *obiter*, at p. 222:

I would have been tempted to hold that all the conditions are unfair and unreasonable for two reasons: first, they are in such small print that one can barely read them; secondly, the draughtsmanship is so convoluted and prolix that one almost needs an LL.B. to understand them. However, neither of those arguments was advanced before me, so I say no more about them.

(p. 320) 7.4.5.1 How should the courts approach this reasonableness requirement and what factors have been relevant in the B2B context?

**George Mitchell (Chester Hall) Ltd v Finney Lock Seeds Ltd**

[1983] 2 AC 803 (HL)

The facts of this case appear at page 304, section 7.3.5.

**Held:** Although, on its true construction, the clause applied to what had happened, it was not fair and reasonable to allow reliance on the clause (within s. 55 of the SGA 1979). A number of factors were stressed, as follows.

(a) It had been the defendants’ practice to settle claims in excess of the limitation if they considered them to be justified. It therefore appeared that the defendants did not always consider the clause to be fair and reasonable.

(b) The defendants could have insured against crop failure without materially increasing the price of the seed.

(c) The supply of incorrect seed was the result of negligence and this was important in relation to the ‘reasonableness’ of the clause.

LORD BRIDGE: My Lords, at long last I turn to the application of the statutory language to the circumstances of the case. Of the particular matters to which attention is directed by paragraphs (a) to (e) of section 55(5), only those in (a) to (c) are...
relevant. As to paragraph (c), the respondents admittedly knew of the relevant condition (they had dealt with the appellants for many years) and, if they had read it, particularly clause 2, they would, I think, as laymen rather than lawyers, have had no difficulty in understanding what it said. This and the magnitude of the damages claimed in proportion to the price of the seeds sold are factors which weigh in the scales in the appellants’ favour.

The question of relative bargaining strength under paragraph (a) and of the opportunity to buy seeds without a limitation of the seedsman’s liability under paragraph (b) were inter-related. The evidence was that a similar limitation of liability was universally embodied in the terms of trade between seedsmen and farmers and had been so for very many years. The limitation had never been negotiated between representative bodies but, on the other hand, had not been the subject of any protest by the National Farmers’ Union. These factors, if considered in isolation, might have been equivocal. The decisive factor, however, appears from the evidence of four witnesses called for the appellants, two independent seedsmen, the chairman of the appellant company, and a director of a sister company (both being wholly-owned subsidiaries of the same parent). They said that it had always been their practice, unsuccessfully attempted in the instant case, to negotiate settlements of farmers’ claims for damages in excess of the price of the seeds, if they thought that the claims were ‘genuine’ and ‘justified.’ This evidence indicated a clear recognition by seedsmen in general, and the appellants in particular, that reliance on the limitation of liability imposed by the relevant condition would not be fair or reasonable.

Two further factors, if more were needed, weight the scales in favour of the respondents. The supply of autumn, instead of winter, cabbage seeds was due to the negligence of the appellants’ sister company. Irrespective of its quality, the autumn variety supplied could not, according to the appellants’ own evidence be grown commercially in East Lothian. Finally, as the trial judge found, seedsmen could insure against the risk of crop failure caused by supplying the wrong variety of seeds without materially increasing the price of seeds.

My Lords, even if I felt doubts about the statutory issue, I should not, for the reasons explained earlier, think it right to interfere with the unanimous original decision of that issue by the Court of Appeal.

As it is, I feel no such doubts. If I were making the original decision, I should conclude without hesitation that it would not
be fair or reasonable to allow the appellants to rely on the contractual limitation of their liability.

1. At pp. 815F–816B, Lord Bridge gave guidance on how the reasonableness question should be approached:

This is the first time your Lordships' House has had to consider a modern statutory provision giving the court power to override contractual terms excluding or restricting liability, which depends on the court's view of what is 'fair and reasonable.' The particular provision of the modified section 55 of the Act of 1979 which applies in the instant case is of limited and diminishing importance. But the several provisions of the Unfair Contract Terms Act 1977 which depend on 'the requirement of reasonableness', defined in section 11 by reference to what is 'fair and reasonable,' albeit in a different context, are likely to come before the courts with increasing frequency. It may, therefore, be appropriate to consider how an original decision as to what is 'fair and reasonable' made in the application of any of these provisions should be approached by an appellate court. It would not be accurate to describe such a decision as an exercise of discretion. But a decision under any of the provisions referred to will have this in common with the exercise of a discretion, that, in having regard to the various matters to which the modified section 55(5) of the Act of 1979, or section 11 of the Act of 1977 direct attention, the court must entertain a whole range of considerations, put them in the scales on one side or the other, and decide at the end of the day on which side the balance comes down. There will sometimes be room for a legitimate difference of judicial opinion as to what the answer should be, where it will be impossible to say that one view is demonstrably wrong and the other demonstrably right. It must follow, in my view, that, when asked to review such a decision on appeal, the appellate court should treat the original decision with the utmost respect and refrain from interference with it unless satisfied that it proceeded upon some erroneous principle or was plainly and obviously wrong.
7. Exemption clauses and unfair contract terms

2. For examples of cases in which an appellate court has overturned a first-instance finding on reasonableness, see *Watford Electronics Ltd v Sanderson CFL Ltd* [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696 (see page 326, section 7.4.5.2), and *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361, [2009] 1 All ER (Comm) 586 (see page 324, section 7.4.5.2).


55 But the question is not whether the clause is, in general, a reasonable clause. The question is whether it was a reasonable clause in the contract made between this vendor and this purchaser at the time when the contract was made.

It is therefore very difficult to give advice on whether a clause is likely to satisfy the reasonableness requirement in s. 11. However, reviewing the case law highlights recurring factors.

R. W. Green Ltd v Cade Brothers Farms

[1978] 1 Lloyd’s Rep 602

The sellers, seed potato merchants, sold to the buyers, who were farmers, 20 tons of uncertified King Edward potatoes at a price of £28 per ton. The sale was made on the standard terms of the National Association of Seed Potato Merchants, clause 5 of which provided that:

> Time being the essence of this Contract … notification of rejection, claim or complaint must be made to the Seller giving a statement of the grounds for such rejection claim or complaint within three days after the arrival of the seed at its destination … It is specifically provided and agreed that compensation and damages payable under any claim or claims arising out of this Contract under whatsoever pretext shall not under any circumstances amount in aggregate to more than the Contract price of the potatoes forming the subject of the claim or claims.

In fact, it was later discovered that the potatoes were infected with a potato virus, which was not discoverable by inspecting the seeds. The sellers brought an action to recover monies owed for seed supplied.
7. Exemption clauses and unfair contract terms

and the buyers counterclaimed to set off against this their loss of profit on the crop (£6,000). The sellers argued that they were protected from such a claim by their conditions of sale and that the buyers could recover only the price of the potatoes (£634).

**Held:** It was not fair and reasonable (within s. 55 of the SGA 1979) to allow reliance on that part of the clause imposing a three-day time limit for complaints, since it was not possible to discover the defect within that time. However, the part of the clause limiting liability to the cost of the potato seeds was reasonable because the parties were of equal bargaining power, the clause had been in use for many years, and it had evolved following trade practice and discussion between the Seed Potato Merchants Association and the National Farmers’ Union. In addition, the buyers could have purchased certified seed at a higher price and would have been guaranteed against the virus.

**GRiffiths J:** This contract, like any commercial contract, must be considered and construed against the background of the trade in which it operates. The plaintiffs’ conditions are based upon a standard form of conditions produced by the National Association of Seed Potato Merchants. They are used by a large majority of seed potato merchants and they have been in use in their present form for over 20 years. They have evolved over a much longer period as the result both of trade practice and discussions between the Association and the National Farmers’ Union. They are therefore not conditions imposed by the strong upon the weak; but are rather a set of trading terms upon which both sides are apparently content to do business ...

On my findings no complaint was made about the potatoes until 13 days after delivery. The plaintiffs therefore say that the claim is out of time and barred by the condition that it must be made within three days of delivery. The plaintiffs’ directors, in their evidence, explained that such a term was necessary in the trade because potatoes are a very perishable commodity and may deteriorate badly after delivery, particularly if they are not properly stored. So it was thought reasonable to give the farmer three days to inspect and make his complaint. This appears to me to be a very reasonable requirement in the case of damage that is discoverable by reasonable inspection. But the presence of virus Y in the potatoes was not discoverable by inspection, and the complaint that was made did not relate to this defect, which neither the farmer nor the potato merchant suspected.
At the time this contract was made no one would expect it to have been practicable for the farmer to complain of virus Y in the potatoes within three days of delivery, for the simple reason that he would not know of its presence. It would therefore, in my judgment, not be fair or reasonable that this claim should be defeated because no complaint was made within three days of delivery. I therefore declare that that part of cl. 5 is unenforceable in this action and provides no defence to the plaintiffs.

Is the claim to be limited to the contract price of the potatoes? … The parties were of equal bargaining strength; the buyer received no inducement to accept the term. True, it appears that he could not easily have bought potatoes without this term in the contract, but he had had the protection of the National Farmers’ Union to look after his interests as the contract evolved and he knew that he was trading on these conditions.

No moral blame attaches to either party; neither of them knew, nor could be expected to know, that the potatoes were infected. There was of course a risk; it was a risk that the farmer could largely have avoided by buying certified seed, but he chose not to do so. To my mind the contract in clear language places the risk in so far as damage may exceed the contract price, on the farmer. The contract has been in use for many years with the approval of the negotiating bodies acting on behalf of both seed potato merchants and farmers, and I can see no grounds upon which it would be right for the Court to say in the circumstances of this case that such a term is not fair or reasonable.

1. A number of the Sch. 2 guidelines were applicable in this case, as follows.
   (a) The parties were of equal bargaining power since, although they contracted on the sellers’ standard terms, these terms had been negotiated by the relevant trade bodies. It was also possible to purchase certified seed and the buyers had chosen not to do so.
   (b) It was not possible to contract for the purchase of uncertified seeds and thus avoid this clause, but this was offset by the factors in (a) above. (p. 323)
   (c) The parties had dealt on these terms for five or six years, and the buyers ought to have been aware of them.
7. Exemption clauses and unfair contract terms

(d) The first part of the clause requiring defects to be notified within three days of delivery is a condition affecting liability, and the test in Sch. 2 condition (d) is whether compliance with this was reasonably practicable. Griffiths J held that it was not.

2. In *Stewart Gill Ltd v Horatio Myer & Co. Ltd* [1992] 1 QB 600 (see page 306, section 7.4.1.1.1), the Court of Appeal refused to sever unreasonable words in a clause when assessing reasonableness. The clause in *R. W. Green v Cade Brothers Farms* does, however, appear to be separable into two distinct issues and is therefore distinguishable. Equally, in *Regus (UK) Ltd v Epcot Solutions Ltd* [2008] EWCA Civ 361, [2009] 1 All ER (Comm) 586, the Court of Appeal commented (*obiter*) that if clauses are seen as independent, i.e. serving different purposes, they can be severed and enforced. As seen earlier in *Goodlife Foods Ltd v Hall Fire Protection Ltd* [2017] EWHC 767 (TCC), [2017] BLR 389 (see page 313, section 7.4.3), this too is the case for a clause purporting to exclude liability for death and personal injury for negligence as well as other risks.

St Albans City and District Council v International Computers Ltd


The claimant, a local authority, had contracted with the defendants for the provision and installation of software to enable the local authority to create a database of eligible payers of the Poll Tax. The software contained an error, so that the figure submitted to central government was overstated and the local authority therefore suffered loss. The local authority brought an action for damages and the defendants sought to rely on a limitation clause in the contract limiting their liability to £100,000. Scott Baker J, at first instance, held that the limitation clause was unreasonable and could not be relied upon.

The following factors were identified as leading to the conclusion that the limitation was unreasonable.

(a) The defendant company was very substantial and, as a wholly owned subsidiary of a multinational, had ample resources to meet any liability.

(b) The defendant company had product liability insurance cover of £50 million and could not justify the limit of liability to £100,000, which was small compared to the potential risk and the actual loss.
7. Exemption clauses and unfair contract terms

(c) The defendant company was in a very strong bargaining position relative to the claimant, since it was one of a limited number of companies capable of fulfilling the local authority’s requirements. The alternative companies also dealt on similar standard conditions.

(d) The practical consequence of a contrary finding of reasonableness would be that the loss would be borne by the local authority’s population, either through increased taxation or reduced services, whereas the defendants were covered by insurance and should carry the risk, since they were the party that stood to make the profit on the contract.

On appeal, the Court of Appeal was mainly concerned with the measure of the damages award and, in part, allowed the appeal on that issue.

Notes

1. These factors outweighed those on the other side of the balance—namely, that this contract was between two ‘businesses’ that should be free to contract on whatever terms they chose, that the local authority was aware of the limitation when it contracted, and that limitations of this kind were commonplace in the industry.

2. Prior to St Albans, it was thought likely that a limitation clause in a contract between two ‘businesses’ would be reasonable in the vast majority of cases. However, the judge in St Albans adopted a protectionist attitude towards the local authority, which, although a ‘business’ within UCTA 1977, was in a distinct position and arguably in greater need of protection than a large public limited company. Clearly, inequality of bargaining power can exist in a B2B contract.

This case can be compared with Southwark London Borough Council v IBM UK Ltd [2011] EWHC 549 (TCC), 135 Con LR 136, in which Akenhead J concluded, obiter, that the exclusion of any statutory implied terms would be reasonable given the equal bargaining power of the parties, the fact that a protracted negotiation had taken place, and that the local authority had achieved some enhancements of the software to suit its requirements.
7. Exemption clauses and unfair contract terms

7.4.5.2 The recent approach to reasonableness in commercial contracts

In Monarch Airlines Ltd v London Luton Airport Ltd [1997] CLC 698 (see page 293, section 7.3.2.1), Clarke J also had to consider whether clause 10 was unenforceable under UCTA 1977. On the facts, s. 2(2) applied, hence the defendant had to establish that the clause satisfied the reasonableness requirement in s. 11. The judge held, at p. 712, that the clause was reasonable at the time that the contract was made:

[The clause] was generally accepted in the market, including the insurance market. Indeed, so far as I am aware, there has been no suggestion in the market (whether it be from the airlines, the airports or the insurers) that the clause be amended in any way. It was accepted by the plaintiff without demur. It has a clear meaning and the insurance arrangements of both parties could be made on the basis that the contract was governed by standard terms which had already been held to be reasonable in principle.

NOTE

For a commercial contract, it should be much easier to establish the reasonableness of the clause, especially if the clause in question is contained in a standard form generally accepted in the industry. This accords with the approach adopted in Photo Production v Securicor [1980] AC 827 (see page 301, section 7.3.5) of non-interventionism, and leaving it to the parties to allocate the risks and responsibility for insurance cover. More recently, in Regus (UK) Ltd v Epcot Solutions Ltd [2008] EWCA Civ 361, [2009] 1 All ER (Comm) 586, it was held that there was nothing unreasonable in a clause limiting liability for loss of profits and consequential losses in a commercial contract, since the parties were of equal bargaining power, had negotiated their contract, and the evidence was that the customer used a similar clause in its own business. Customers were advised to take out insurance to cover their business losses, and it was generally more appropriate for the customer to take out this insurance than the service supplier. Insurance was again an important factor in assessing the reasonableness of the clause in Goodlife Foods Ltd v Hall Fire Protection Ltd [2018] EWCA Civ 1371. Two particular factors underlie the importance of insurance: first the identity of the party best placed to take out insurance and, secondly, the manner in which the clause was drafted (at [76]-[77]).

In Granville Oil & Chemicals Ltd v Davies Turner & Co. Ltd [2003] EWCA Civ 570, [2003] 1 All ER (Comm) 819, Tuckey LJ (with whose judgment
7. Exemption clauses and unfair contract terms

Potter LJ and Hart J agreed) made the following comment on the s. 11 discretion in commercial contracts:

[31] ... I am less enthusiastic about its [the 1977 Act’s] intrusion into contracts between commercial parties of equal bargaining strength, who should generally be considered capable of being able to make contracts of their choosing and expect to be bound by their terms.

This statement is now cited with approval as a matter of course in the context of commercial contracts involving an assessment of reasonableness. This non-interventionist approach was recently reasserted in Goodlife Foods Ltd v Hall Fire Protection Ltd [2018] EWCA Civ 1371 where the Court of Appeal reiterated its support for party autonomy and freedom of contract, especially where the parties are of equal bargaining power (at [103]). This non-interventionist approach highlights the judicial view that exclusion clauses are, on a construction basis, used as tools to allocate risk.

Schenkers Ltd v Overland Shoes Ltd

[1998] 1 Lloyd’s Rep 498 (CA)

The claimants, freight forwarders, had contracted with the defendants, shoe importers, on the British International Freight Association (BIFA) standard trading conditions. Clause 23(A) of these conditions was a ‘no set-off clause’ in the following terms:

The Customer shall pay to the Company in cash ... all sums immediately when due, without reduction or deferment on account of any claim, counterclaim or set-off.

The defendants sought to set off a sum for value added tax (VAT), which they claimed that the claimants should have reclaimed for the benefit of the defendants. The claimants sought to rely on clause 23(A). The defendants claimed that it was unreasonable to exclude the right of set-off, that the clause had not been relied upon in practice in their long course of previous dealings, and that they were in a position of unequal bargaining power.

Held: The claimants had proved the clause was reasonable within s. 3 of UCTA 1977.
PILL LJ: In my judgment the plaintiffs have satisfied the burden upon them of establishing that cl. 23(A) in the circumstances satisfies the requirement of reasonableness. The clause was in common use and well known in the trade following comprehensive discussions between reputable and representative bodies mindful of the considerations involved. It reflects a general view as to what is reasonable in the trade concerned. It was sufficiently well known that any failure by the defendant’s officers, in the course of long and substantial dealings, to put their minds to the clause cannot be relied on to establish that it was unfair or unreasonable to include it in the contracts ... In a situation in which there was no significant inequality of bargaining position, the customs of the trade were an important factor. The parties were well aware of the circumstances in which business was conducted, the heads of expenditure to be incurred and the risks involved.

In present circumstances, I see little merit in the defendants’ argument that the clause had not in practice been relied upon. The give and take practised by the parties in the course of substantial dealings upon the running account was admirable and conducive to a good business relationship but did not in my judgment prevent the plaintiffs, when the dispute arose, relying upon the term agreed. In George Mitchell, there was evidence that neither party expected the limitation of liability clause to [be] applied literally and a recognition that reliance on the clause was unreasonable. While there was evidence in the present case that there was no ready or frequent resort to the clause, there was no such recognition. I cannot find conduct which permits the defendants to claim that reliance on the clause would be unfair or unreasonable.

1. Significantly, having regard to the scale of the defendants’ operation and the fact that the freight forwarding market in Far East trade was very competitive, the Court of Appeal rejected the defendants’ argument that it was in a position of unequal bargaining power. (p. 326)

2. It is highly relevant that the Court of Appeal chose to distinguish George Mitchell regarding the lack of previous reliance on the clause. This, and the trends in recent case law, indicates that the court’s approach to reasonableness in the context of commercial contracts is nearer to the Photo
The central case cited in support of the non-interventionist approach to exemption clauses in commercial contracts is the following decision of the Court of Appeal.

**Watford Electronics Ltd v Sanderson CFL Ltd**

**[2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696 (CA)**

A contract for the supply of a bespoke integrated software system included (i) a clause purporting to exclude any liability for indirect or consequential losses and (ii) a clause limiting liability in a general sense to the price paid under the contract (£104,600). The system was faulty and the claimant sought damages for breach of contract amounting to £5.5 million, for loss of profits, the increased costs of working, and reimbursement of the cost of a replacement software system. At first instance, the judge held that the exemption clauses were unreasonable in their entirety.

**Held (on appeal):** The clauses were reasonable having been negotiated by two experienced business people who represented substantial companies of equal bargaining power.

CHADWICK LJ [with whom Peter Gibson LJ and Buckley J agreed]: Was the term a fair and reasonable one to be included?

49 ... I am satisfied that this is a case in which, if this court takes a different view from that of the judge on the question whether the inclusion of the limit of liability clause in Sanderson's standard terms and conditions was fair and reasonable having regard to the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made, it is entitled to give effect to its own view. That is because I am satisfied that the judge reached his conclusion on the wrong basis.

50 ... [O]n a true analysis of the limit of liability clause, it comprises two distinct contract terms in relation to which it is necessary to consider whether the requirement of reasonableness is satisfied. One (to which I shall refer for convenience as 'the term excluding indirect loss') is that contained in the first sentence of the clause. The other ('the term limiting direct loss') is contained in the second sentence.
It is, I think, appropriate to consider, separately in relation to each term, whether the requirement of reasonableness is satisfied; although, of course, in considering whether that requirement is satisfied in relation to each term, the existence of the other term in the contract is relevant.

51 I turn, therefore, to consider whether the requirement of reasonableness is satisfied in relation to the term excluding indirect loss. It is important to keep in mind (i) that, as a matter of construction, the term does not seek to exclude loss resulting from pre-contractual statements in relation to which a claim lies (if at all) in tort or under the 1967 Act and (ii) that the term is qualified by the addenda so that it does not exclude indirect or consequential loss resulting from breach of warranty unless Sanderson has used its best endeavours to ensure that the equipment and the software does comply with the warranty.

52 I accept that the court is required to have regard, in the present case, to the ‘guideline’ matters set out in Schedule 2 to the 1977 Act. There are factors, identified by the guidelines, which point to a conclusion that the term excluding indirect loss was a fair and reasonable one to include in this contract. The parties were of equal bargaining strength; the inclusion of the term was, plainly, likely to affect Sanderson’s decision as to the price at which was [sic] prepared to sell its product; Watford must be (p. 327) taken to have appreciated that; Watford knew of the term, and must be taken to have understood what effect it was intended to have; the product was, to some extent, modified to meet the special needs of the customer. Other factors point in the opposite direction. The judge found that, although there were other mail order packages on the market, Mailbrain was the only one which appeared to fulfil Watford’s needs ...; and, further, that Watford could not reasonably have expected to have been able to have acquired a similar software package, if available, on better terms as to performance and as to the supplier’s potential liability for non-performance.

53 I do not, for my part, accept that the term excluding indirect loss is a term to which s. 11(4) of the 1977 Act applies. It is not, I think, properly to be regarded as a term by which a person (Sanderson) seeks to restrict liability to a specified sum of money; rather the term seeks to exclude liability for indirect or consequential loss altogether, in those circumstances in which it is intended to have effect. Nevertheless, it seems to me right to have regard, as part of the circumstances which were, or ought reasonably to have been, known to or in the contemplation of the parties when the contract was made, both to the resources which could be expected to be available to each party for the purpose of meeting indirect or consequential loss resulting from the failure of the equipment or software to
7. Exemption clauses and unfair contract terms

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<td>perform in accordance with specification, and to the possibility that such loss could be covered by insurance.</td>
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54 It seems to me that the starting point in an enquiry whether, in the present case, the term excluding indirect loss was a fair and reasonable one to include in the contract which these parties made is to recognise (i) that there is a significant risk that a non-standard software product, ‘customised’ to meet the particular marketing, accounting or record-keeping needs of a substantial and relatively complex business (such as that carried on by Watford), may not perform to the customer’s satisfaction, (ii) that, if it does not do so, there is a significant risk that the customer may not make the profits or savings which it had hoped to make (and may incur consequential losses arising from the product’s failure to perform), (iii) that those risks were, or ought reasonably to have been, known to or in the contemplation of both Sanderson and Watford at the time when the contract was made, (iv) that Sanderson was in the better position to assess the risk that the product would fail to perform but (v) that Watford was in the better position to assess the amount of the potential loss if the product failed to perform, (vi) that the risk of loss was likely to be capable of being covered by insurance, but at a cost, and (vii) that both Sanderson and Watford would have known, or ought reasonably to have known, at the time when the contract was made, that the identity of the party who was to bear the risk of loss (or to bear the cost of insurance) was a factor which would be taken into account in determining the price at which the supplier was willing to supply the product and the price at which the customer was willing to purchase. With those considerations in mind, it is reasonable to expect that the contract will make provision for the risk of indirect or consequential loss to fall on one party or the other. In circumstances in which parties of equal bargaining power negotiate a price for the supply of product under an agreement which provides for the person on whom the risk of loss will fall, it seems to me that the court should be very cautious before reaching the conclusion that the agreement which they have reached is not a fair and reasonable one.

55 Where experienced businessmen representing substantial companies of equal bargaining power negotiate an agreement, they may be taken to have had regard to the matters known to them. They should, in my view, be taken to be the best judge of the commercial fairness of the agreement which they have made; including the fairness of each of the terms in that agreement. They should be taken to be the best judge on the question whether the terms of the agreement are reasonable. The court should not assume that either is likely to commit his
company to an agreement which he thinks is unfair, or which he thinks includes unreasonable terms. Unless satisfied that one party has, in effect, taken unfair advantage of the other—or that a term is so unreasonable that it cannot properly have been understood or considered—the court should not interfere.


59 In my judgment, the starting point in the consideration of the question of reasonableness is that the Agreements were made between commercial organisations and in a commercial context. Admittedly, AXA was an immeasurably larger organisation than the companies with which it contracted, and the guarantors of the companies’ liabilities were, I assume, persons of modest means. However, as financial advisors, they were accustomed to deal with written agreements, such as insurance and pension policies, and I think it fair to assume that they would generally, if not always, advise their clients to ensure that they were content with the written terms of their policies. I would therefore have expected the Defendants to have read the Agreements, and in the case of the individual Defendants the guarantees that they signed.

60 … The contractual provisions in issue are not unusual in the insurance industry: the evidence before the judge was that they are standard terms. Two of the company Defendants … had entered into previous agreements with AXA on materially identical terms.

2. Although the Court of Appeal in Watford Electronics had emphasized that commercial men ‘should be taken to be the best judge of the commercial fairness of each of the terms of the agreement’, it does not follow that an exemption clause in such a contract can never be unreasonable. For example, in Overseas Medical Supplies Ltd v Orient Transport Services Ltd [1999] CLC 1243, the defendant was protected by a limitation clause if it lost the equipment it was transporting. However, it was also a term of the contract that the defendant was to insure this equipment and the defendant had failed to do this. It was held that, although the limitation of liability was reasonable in
relation to loss of the goods, it was unreasonable in respect of the loss arising through the failure to insure. It is therefore necessary to evaluate the overall purpose and effect of the clauses.

*Trustees of Ampleforth Abbey Trust v Turner & Townsend Management Ltd* [2012] EWHC 2137 (TCC), [2012] TCLR 8, concerned a limitation clause in a contract engaging a project management company, which provided that liability for negligence should be limited to the liability covered by the professional indemnity policy, but also stated that liability was to be limited to the fees paid (in this case, £111,321). The judge held this clause to be unreasonable, since the company was required by the contract to take out indemnity insurance for £10 million. The clauses were internally incompatible.

3. Other case examples have stressed the realities of a lack of equal bargaining power. For example, in *Motours Ltd v Euroball (West Kent) Ltd* [2003] EWHC 614 (QB), [2003] All ER (D) 165, the judge avoided the non-interventionist approach advocated for commercial contracts and concluded that a clause in standard conditions of a telephone service supplier excluding liability for consequential losses was unreasonable. He concluded that the parties were not of equal bargaining power and there had been no discussion or negotiations about the terms of the contract.

In *Barclays Bank plc v Grant Thornton* [2015] EWHC 320 (Comm), [2015] 2 BCLC 537, Cooke J at [91] appeared to draw a distinction between the approach in commercial contracts where the contracting parties were both major commercial concerns and the approach where one commercial concern was a small company: ‘The court here can be confident of its answer in circumstances where sophisticated business parties are able to protect their own interests and do not require the protection of the 1977 Act in the same way as small companies … ’. This is likely to become an important distinction in terms of interpretation of UCTA reasonableness post the CRA 2015.

4. It would appear that, in the context of the supply of computer software, an exclusion of consequential loss will be reasonable if the contract permits some recovery for direct loss, such as a money-back guarantee.

The underlying explanation of the finding of reasonableness of the exemption covering consequential losses in computer software contracts is disclosed in the ‘soft drinks’ cases—namely, the nature of the risk and the scope of the potential liability.

The ‘soft drinks’ cases concerned the supply of carbon dioxide to manufacturers of soft drinks, where that supply was found to be contaminated with traces of benzene. In *Britvic Soft Drinks v Messer UK*
7. Exemption clauses and unfair contract terms

In Britvic, Mance LJ criticized the approach of the judge at first instance on the assessment of reasonableness and distinguished Watford Electronics.

MANCE LJ: 21 The Judge accepted that the parties were to be regarded as having been of equal bargaining power—see par. (a) in Sch 2 to the Act. There were other suppliers (Hydrogas and BOC) to which THP and Brothers could have gone. The Judge also treated it as axiomatic for the purposes of par. (c) that ‘on the footing that the terms are applicable at all’ the buyers ‘must be regarded as cognizant of their existence and effect’. I am not satisfied that par. (c) can be quite so easily disposed of. Contractual incorporation may in some circumstances occur without a party either knowing, or being realistically in a position where he or it can be blamed for not knowing, of the extent of certain terms. Take someone contracting for the carriage of a parcel by rail or air on the carriers’ standard conditions. No-one really expects him to obtain or read the terms. Nor do I think that par. (c) is to be necessary even to be read as equating the positions of someone who actually knows and someone who ‘ought reasonably to have known’ of the existence and extent of a term. It seems to me legitimate to consider and take into account the actual extent and quality of the knowledge of a party, however much he or it may, under ordinary contractual principles, have become contractually bound by the particular term(s).

22 Thus, in the case of Watford Electronics Ltd v Sanderson CFL Ltd [2001] EWCA Civ 317, [2001] 1 All ER (Comm) 696, cited to the Judge and to us, the Judge found as a relevant factor under par. (c) that the buyer of the relevant software was—

... aware of the existence of the term, only first learned of its existence towards the end of the pre-contract discussions, attempted unsuccessfully to have it substantially amended, only succeeded in achieving a make-weight amendment and learnt from Sanderson [the supplier] that a term excluding liability was standard software industry practice.
7. Exemption clauses and unfair contract terms

23 The Court of Appeal in *Watford*, in upholding the validity of an exclusion of liability for any ‘claims for indirect or consequential losses whether arising from negligence or otherwise’, regarded that as a most material factor, as appears from the judgment given by Lord Justice Chadwick (with which Mr Justice Buckley agreed) at pars. 54(vii) and 56 and that of Lord Justice Peter Gibson at par. 62(4). In the present case, the commercial and contractual background were significantly different. The manufacture of carbon dioxide so as to exclude benzene does not compare with the provision of software (an exercise notoriously liable to give rise to problems). No-one would have contemplated that the manufacturing process would allow benzene in, or (despite cl 11.2) that the buyers (THP and Brothers) would test for benzene, or indeed for compliance with BS 4105, which Messer anyway warranted. The parties did not discuss or negotiate with regard to the specific provisions of the contract, cl 11.1 and 11.2 in particular. Clauses 11.1 and 11.2 were simply incorporated as part of Messer’s standard provisions. Although this is not a consideration specifically identified in Schedule 2 [to the 1977 Act], it seems to me that it can be relevant under par. (c) and anyway as a general consideration under s. 11(2) (cf also by analogy s. 3(1)).

Thus the fact that the contamination of the carbon dioxide would not have been contemplated was a reason favouring acceptance of liability rather than a reason favouring the reasonableness of exclusion of that liability.

It was also considered important in *Bacardi-Martini* that the contamination was the result of a manufacturing error and it was considered that the supplier ought not to be able to transfer responsibility for that risk to the buyer. The same might be said of defective computer software, but it appears to be accepted that such defects are considerably more likely, and therefore it is appropriate and reasonable at least to limit liability.

The question of the appropriateness of the risk allocation can be seen in recent case law concerning exemption clauses in commercial contracts. For example, in *Sterling Hydraulics Ltd v Dichtomatik Ltd* [2006] EWHC 2004 (QB), [2007] 1 Lloyd’s Rep 8 (see page 234, Chapter 6, section 6.3.1.2), there were clauses that attempted to exclude all liability for defects in the seals—in particular for consequential loss—other than where there was either prompt reporting of defects, in which event liability would be limited to the price of the goods, or the supplier had been intentionally or grossly negligent. However, apart from the imposition of a one-week time limit for reporting claims based on hidden defects, the exclusion and limitation provisions were considered to be reasonable in view of the equal bargaining power. Limitation to the price was reasonable because it was a ‘low value high volume contract’ and,
7. Exemption clauses and unfair contract terms

since the supplier was given no information as to the precise use for the
seals, it could not have taken out insurance for the full risks.

This decision can be compared with Balmoral Group Ltd v Borealis (UK)
220, which held that, since the clause required Balmoral to bear the
entire risk of latent defects in Borealis’s product, it was unreasonable and
an inappropriate allocation of the risk. Balmoral had no choice other than
to accept Borealis’s terms and Borealis could have covered the risk in
relation to its own products with insurance.

CHRISTOPHER CLARKE J: 421 When the contracts were made
Borealis knew that Balmoral was buying borecene for the purpose
of making oil tanks and that it was relying on Borealis to supply a
polymer capable of being used to make consistently satisfactory
tanks. It was the assumption of both sides that it was so capable.
The supply of a product which, because of a latent defect ... made
the manufacture of consistently satisfactory tanks impossible would
confound those assumptions. In those circumstances a blanket
exclusion of any liability whatever is prima facie unreasonable (as
was the exclusion of any liability for the supply of carbon dioxide
with an excessive benzene content in Britvic Soft Drinks Ltd v
Messer UK [2002] 2 Lloyd’s Rep 368; and Bacardi-Martini
Beverages v Thomas Hardy Packaging Ltd [2002] 2 Lloyd’s Rep
379). I do not regard the supply of product with a latent defect as
so remote a contingency that it ought to play no weight in
determining the reasonableness of the exclusion. Nor were these
contracts in respect of which there were notorious difficulties in
successful performance or a high risk of failure.

422 A determination of the reasonableness of a contractual
exclusion requires consideration of whether the allocation of risk
effected by the exclusion is appropriate. I have not been persuaded
that requiring Balmoral to bear the entire risk of a latent defect in
Borealis’ product is an appropriate allocation of risk. The Sale of
Goods Act itself recognises that, all other things being equal, it
should be the seller who bears the responsibility. Borealis has
extensive insurance against just such a risk. Whilst product recall
insurance would probably have been available to Balmoral, albeit
expensively, Balmoral did not have such insurance. The evidence
does not establish that product recall insurance would have been
normal for someone in Balmoral’s position.

423 But commercial parties habitually make agreements amongst
themselves that allocate risk; and the court should not lightly treat
such agreements as unreasonable. The present case is not,
however, one in which the contracts made were the result of a
serious negotiation as to the incidence of risk: cf the Watford case
where that was exactly what took place. Borealis’ terms were
presented on a take-it-or-leave-it basis and Balmoral’s scope for going elsewhere on any better terms was very limited … Whilst Borealis UK’s terms were standard in the trade they are not the product of any agreed process of negotiation between representatives of sellers and buyers.

424 I take into account the submissions made by Borealis … as to the extent of their potential liability and the cost implications of their being potentially liable for claims in respect of unfitness for any of the many purposes for which borecene might be bought. In respect of these submissions (p. 331) two matters strike me as of particular relevance. First, whilst liability for fitness for purpose can be onerous it is not unqualified. It only arises when the buyer reasonably relies on the seller and the goods are not reasonably fit for what the seller knows is their intended purpose. The defect must be one that lies within the seller’s sphere of expertise. The seller can, of course, still be liable for a latent defect of which he is himself unaware. But, as between seller and buyer, it is more appropriate that loss from such a defect should be borne by the seller. As Scott Baker, J, as he then was, said in St Alban’s City and District Council v International Computers Ltd [1995] FSR 686 it is not unreasonable that he who stands to make the profit should carry the loss. Borealis is a very large organisation, much larger than Balmoral both in term of assets and technical expertise, and has insurance against liabilities such as these. It can spread the cost of that insurance, and of any exposure not covered by insurance, over a very wide range of purchasers. Balmoral might be able to pass on the cost of product recall insurance but whether that is so is, on the present evidence, an open question.

425 It is material also to look at the consequences. If borecene was, contrary to my findings, not suitable for making oil tanks because of a latent defect, Balmoral will have suffered a huge loss (a foreseeable consequence of such a defect) which they had no real opportunity to avoid at the manufacturing stage. It is not reasonable that they should be without any redress from the manufacturer at all.

426 Lastly, it is not without significance that Borealis settled some of Balmoral’s claims, without reference to Borealis’ conditions. That cannot automatically mean that reliance on the impugned terms would have been unreasonable, or that the terms themselves were unreasonable. But, especially when the settlement is as high as £170,000, it is an indication to that effect.

7.5 Clause in a B2C contract must not be rendered unenforceable by Part 2 of the Consumer Rights Act 2015
7. Exemption clauses and unfair contract terms

7.5.1 Background to, and the general scope of, the Act

Directive 93/13/EEC on Unfair Terms in Consumer Contracts was originally implemented in English law by the Unfair Terms in Consumer Contracts Regulations 1994, SI 1994/3159, which substantially reproduced the wording, if not the order of presentation, of the Directive itself. The 1994 Regulations were repealed and replaced by the Unfair Terms in Consumer Contracts Regulations (UTCCR) 1999, SI 1999/2083. There is now a unified regime for consumer regulations under Part 2 of the CRA 2015. Although the UTCCR 1999 have been repealed in their entirety, as the language of Directive 93/13 is largely preserved in the 2015 Act, case law based on the UTCCR will have continuing relevance for the interpretation of many of the provisions contained in Part 2 CRA 2015 and must therefore be considered.

Whereas the UCTA 1977 regulation in the B2B context is limited to exemption clauses, i.e. clauses which purport to exclude or limit liability or remedies (as further extended by s. 13 UCTA 1977), the regulation in the consumer sphere is far more extensive since it applies to ‘unfair terms’ which are not regarded by the legislation as ‘core terms’.

(p. 332) 7.5.2 When does the Act apply?

Consumer Rights Act 2015

61 Contracts and notices covered by this Part

(1) This Part applies to a contract between a trader and a consumer.

(2) This does not include a contract of employment or apprenticeship.

(3) A contract to which this Part applies is referred to in this Part as a ‘consumer contract’.

The section also states that in addition to ‘terms’ in consumer contracts, this Part also covers ‘consumer notices’.

2 Key definitions

(2) ‘Trader’ means a person acting for purposes relating to that person’s trade, business, craft or profession, whether acting personally or through another person acting in the trader’s name or on the trader’s behalf.

(3) ‘Consumer’ means an individual acting for purposes that are wholly or mainly outside that individual’s trade, business, craft or profession.
7. Exemption clauses and unfair contract terms

**A trader claiming that an individual was not acting for purposes wholly or mainly outside the individual's trade, business, craft or profession must prove it.**

Technically, a sole trader is an individual and it might be necessary to determine whether they are ‘acting for purposes that are wholly or mainly outside’ their trade, business, craft, or profession.

The ‘purpose’ (or intention) is important and a decision under the UTCCR 1999 may be of assistance in making the distinction where the contract is made by an individual sole trader, albeit that the definition of a ‘consumer’ in the CRA 2015 does not require that the consumer be acting wholly for non-business purposes whereas the UTCCR 1999 definition did require this.

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**Overy v Paypal (Europe) Ltd**

**[2012] EWHC 2659 (QB), [2013] Bus LR D1**

An individual had applied to use Paypal’s electronic payment services to collect competition entry fees (the competition prize being his house). He had indicated that the payment service was required for business purposes, because this enabled payments to be made to him directly, but had supplied a mixture of personal details and details of his photography business on the application form. Could he seek the protection of the UTCCR 1999 when the defendant cancelled his access to the services? Did he qualify as a ‘consumer’ within reg. 3 UTCCR 1999 which required him to act ‘for purposes which were outside his trade, business or profession’?

**Held:** A contract would be treated as having been concluded for a purpose outside the person’s business, trade, or profession only if this business purpose were insignificant or negligible and the focus was on satisfying the consumer’s needs in terms of private consumption. Although the claimant’s purpose in opening the account was outside his business or profession, he also intended to use the account for payments relating to his photography business and so could not be a consumer. The judge also stressed the nature of the representations made when opening the account. The claimant was therefore acting for business purposes.

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JUDGE HEGARTY QC (sitting as a High Court judge): 172 I turn, therefore, to consider the preliminary question itself as to whether the 1999 Regulations apply to the agreement made on 22 January 2007 between Mr Overy and Paypal. As I have
previously held, a major purpose for which he opened the account with Paypal was to facilitate the disposal of the property which was his home by means of the competition which he was in the process of organising. It was submitted by [counsel] on behalf of Paypal that this was not in itself a purpose which was outside his trade, business or profession. [Counsel] contended that it should be categorised as a business venture, even though it was limited to the disposal of a single asset by means of a single transaction or linked series of transactions. It was intended, he submitted, to obtain for Mr Overy what would, in effect, be a trading profit over and above the price that he could have expected to receive on a sale in the open market by conventional means. Mr Overy, on the other hand, contended that he was a photographer by profession, and not an estate agent, so that his competition could not properly be regarded as an activity which fell within the activities of his trade, business or profession.

173 For reasons which I have already stated, I do not consider that this question can be answered simply by seeking to categorise Mr Overy’s normal business activities and then asking whether this particular venture fell within the scope of such activities. An individual may be involved in more than one, perhaps many different, trading activities at the same time, some or all of which may overlap. Furthermore, I can see no reason why a single business venture cannot be taken into account in determining whether a particular contract is one to which the 1999 Regulations apply. So it is no answer, certainly no definitive answer, for Mr Overy simply to assert that he was a photographer and not an estate agent.

174 In the end, the question is a matter of fact and degree which has to be resolved by an application of the wording adopted by the 1999 Regulations and of the underlying Directive, assisted by the gloss placed upon that test by the Court of Justice in the *Benincasa v Dentalkit Srl* (Case C-269/95) [1997] ECR I-3767; [1998] All ER (EC) 135. I have come to the conclusion that the competition was not an adventure in the nature of trade. It involved the sale or realisation of a property which he and his wife occupied as their personal residence, albeit by wholly unorthodox means which he designed in order to maximise the amount which he was likely to realise on the disposal of the property. In principle, it seems to me to be little different from a disposal of the same asset by public auction, which itself differs from a private sale through an estate agent only in the means chosen to achieve the sale. I take the view, therefore, that, if this had been the sole purpose for which Mr Overy had opened the PayPal
account, it would have been a purpose outside any trade, business or profession in which he was involved.

175 But, as I have previously found, that was not the only purpose for which Mr Overy opened his Paypal account. I am satisfied that it was also intended to facilitate the receipt of payments for goods and services which he provided in connection with his photography and videography business. To that extent, therefore, when he entered into the contract with Paypal on 22 January 2007, he was not acting for purposes which were outside his trade, business or profession. Furthermore, in my judgment, that purpose could not reasonably be regarded as one which was insignificant or negligible. Accordingly, in view of the principles which I have attempted to summarise earlier in this judgment, he was not entitled to the protection of the 1999 Regulations.

176 But, even if I were wrong in the foregoing conclusion, I am quite satisfied that this is a case in which he would be disentitled from relying upon the 1999 Regulations, even if his purpose had in fact been wholly outside his trade, business or profession. In my judgment, by the nature of the application which he made to Paypal online and the information which he provided in so doing, he clearly conducted himself in such a way as to lead to the obvious conclusion that he was acting in his trade or professional capacity.

7.5.3 The assessment for fairness and terms and notices which are excluded from that assessment

Consumer Rights Act 2015

62 Requirement for contract terms and notices to be fair

(1) An unfair term of a consumer contract is not binding on the consumer.
(2) An unfair consumer notice is not binding on the consumer.
(3) This does not prevent the consumer from relying on the term or notice if the consumer chooses to do so.
(4) A term is unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties’ rights and obligations under the contract to the detriment of the consumer.
7. Exemption clauses and unfair contract terms

(5) Whether a term is fair is to be determined—
(a) taking into account the nature of the subject matter of the contract, and
(b) by reference to all the circumstances existing when the term was agreed and to all of the other terms of the contract or of any other contract on which it depends.
...

(8) This section does not affect the operation of—
(a) section 31 (exclusion of liability: goods contracts),
(b) section 47 (exclusion of liability: digital content contracts),
(c) section 57 (exclusion of liability: services contracts),
or
(d) section 65 (exclusion of negligence liability).

63 Contract terms which may or must be regarded as unfair

(1) Part 1 of Schedule 2 contains an indicative and non-exhaustive list of terms of consumer contracts that may be regarded as unfair for the purposes of this Part.

Notes

1. Section 62 is the key to the control mechanism adopted by Directive 93/13—unfair terms— which introduced the concept of good faith into English law. The key notion is a ‘significant imbalance in the parties’ rights and obligations arising under the contract’ that is in some way contrary to the ‘requirement of good faith’. These are vague and ill-defined criteria, and the CRA 2015 fails to make clear the relationship between them. In particular, following the drafting of s. 62(4), it is unclear whether the requirement of lack of good faith is additional to the condition of imbalance between the parties, or whether imbalance is to be regarded in itself as evidence of a lack of good faith. The general principles contained in s. 62(5) are limited. Consequently, identification of the criteria for compliance with the terms of the Act is a process of deduction from what is termed, in s. 63(1), an ‘indicative and non-exhaustive list of terms ... that may be regarded as unfair’ and which is contained in Sch. 2, Part 1 of the CRA 2015. Twenty 'items' are listed. There is also a small, but significant, body of case law under the UTCCR which may assist in terms of application (see page 336, section 7.5.4).
2. An unfair term is not binding on the consumer at the consumer’s option. However, by s. 67 ‘the contract continues, so far as practicable, to have effect in every other respect’, i.e. the unfair term may be severable.

3. Under s. 62(8) it is impossible to exclude liability for breach of the entrenched rights in a consumer contract. Thus, the terms providing for the goods in a consumer sale of goods to be of satisfactory quality, fit for purpose, and corresponding to description and sample etc., cannot be excluded or restricted (s. 31 CRA 2015). This clarifies one area of uncertainty that used to exist under the UTCCR 1999 (i.e. although the old s. 6(2) SGA 1979 stated that it was not possible to exclude or restrict the satisfactory quality term in a consumer contract, the term would still have needed to be shown to be unfair under the UTCCR 1999). This is no longer the case.

Consumer Rights Act 2015

65 Bar on exclusion or restriction of negligence liability

(1) A trader cannot by a term of a consumer contract or by a consumer notice exclude or restrict liability for death or personal injury resulting from negligence.

NOTE

Section 65 mirrors s. 2(1) UCTA 1977 and provides that (with some exceptions such as an insurance contract and certain liability of occupiers, s. 66) a term or notice cannot exclude or restrict liability for death or personal injury resulting from negligence. This is crucial because under the UTCCR 1999, terms which sought to exclude or restrict liability in negligence for death or personal injury were not barred automatically but subjected to the fairness test. Where the term seeks to exclude or restrict other loss or damage, e.g. death or personal injury which does not result from negligence, or financial loss resulting from negligence, it is subject to the fairness test.

Consumer Rights Act 2015
71 Duty of court to consider fairness of term

(1) Subsection (2) applies to proceedings before a court which relate to a term of a consumer contract.
(2) The court must consider whether the term is fair even if none of the parties to the proceedings has raised that issue or indicated that it intends to raise it.
(3) But subsection (2) does not apply unless the court considers that it has before it sufficient legal and factual material to enable it to consider the fairness of the term.

NOTE

The critical issue pertaining to the s. 62 fairness test relates to where the burden of proof on this matter lies. Under the UTCCR 1999, the burden of proving unfairness was on the consumer. The Law Commission had proposed the reversal of this burden of proof. However, nothing is stated explicitly in the Act to indicate a reversal of this burden. Section 71 CRA 2015 may provide the explanation in the new statutory acceptance that the court has a duty to consider whether a term is fair. This might imply that the ‘fairness test’ would now be determined by the court rather than relying specifically on the consumer to establish it, i.e. the court would look at all the evidence to determine whether the term was fair and permitted.

Consumer Rights Act 2015

64 Exclusion from assessment of fairness

(1) A term of a consumer contract may not be assessed for fairness under section 62 to the extent that—
(a) it specifies the main subject matter of the contract, or
(b) the assessment is of the appropriateness of the price payable under the contract by comparison with the goods, digital content or services supplied under it.

(2) Subsection (1) excludes a term from an assessment under section 62 only if it is transparent and prominent.
(3) A term is transparent for the purposes of this Part if it is expressed in plain and intelligible language and (in the case of a written term) is legible. (p. 336)
7. Exemption clauses and unfair contract terms

(4) A term is prominent for the purposes of this section if it is brought to the consumer’s attention in such a way that an average consumer would be aware of the term.

(5) In subsection (4) ‘average consumer’ means a consumer who is reasonably well-informed, observant and circumspect.

(6) This section does not apply to a term of a contract listed in Part 1 of Schedule 2.

Notes

1. The CRA 2015 excludes certain (so-called ‘core’) terms, potentially within the scope of the Act, from any assessment of their fairness under s. 62. Yet, the terms listed in Part 1 of Sch. 2 will always be subject to such an assessment since ‘they may be regarded as unfair’ (s. 63(1), emphasis added).

2. This apart, s. 64 excludes from this assessment any term which is transparent and prominent (i.e. not hidden in the small print) and which ‘specifies the main subject matter of the contract’. It is also not possible to assess the price term where the assessment for fairness would involve assessing ‘the appropriateness of the price payable … by comparison with the goods, digital content or services supplied under it’. However, when assessing price terms under the UTCCR 1999, reg. 6(2), the courts had drawn a not altogether convincing distinction between ‘core’ terms relating to the price (which could not be assessed) and ‘ancillary’ price terms, which could be assessed for fairness because they fell outside the exclusion from assessment in reg. 6(2). The intention behind the slightly adapted wording in s. 64(1) CRA 2015 is to distinguish between ‘the price’ and ‘aspects of the price other than the amount’, e.g. such as provisions concerned with the timing of the payment or cancellation rights for non-payment, and to eliminate the concept of ancillary terms relating to the price amount or any aspect of calculating the price.

7.5.4 Case law explaining the operation of the Unfair Terms in Consumer Contracts Regulations

7.5.4.1 Director General of Fair Trading v First National Bank plc
7. Exemption clauses and unfair contract terms

[2001] UKHL 52, [2002] 1 AC 481 (HL)

A term in a consumer loan agreement provided for interest to be paid at the contractual rate on sums owing both before and after any judgment. Thus, if judgment on the debt were obtained, interest at the contractual rate would remain payable until the judgment was discharged, despite the fact that all of the instalments due under the judgment had been paid. A debtor might budget for, and pay, judgment instalments only to discover that he owed a further sum in interest. The Director General of Fair Trading considered that this term was ‘unfair’ and sought an injunction to prevent its continued use. The case concerned the 1994 version of the Regulations.

The bank claimed that: (i) the Regulations had no application to the term in question, because it was a ‘core term’ defining the main subject matter of the contract, or concerning the adequacy of the price or remuneration (reg. 3(2) UTCCR 1994, later reg. 6(2) of the UTCCR 1999 and the equivalent provision can be found in CRA 2015, s. 64(1) and (2)—see pages 335–6); and (ii), in any event, the term was not unfair.

The judge at first instance had considered that the term was not a ‘core term’ and that it was not unfair. Although the Court of Appeal agreed that it was not a ‘core term’, it overturned that decision because it considered the term to be unfair in view of the element of unfair surprise for the debtor.

Held (on appeal to the House of Lords):

(a) The term did not fall within reg. 3(2)(b), because it was an incidental term setting out the consequences of a borrower’s default. The term did not concern the adequacy of the interest earned by the bank as remuneration for the loan and so did not express the substance of the parties’ bargain. Accordingly, the Regulations applied to the term.

(b) The term was not unfair within the test prescribed in the Regulations and contained nothing detrimental to the consumer.

LORD BINGHAM [with whose reasons the other members of the House of Lords agreed]:

(1) The applicability of the Regulations

...
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entitling the bank to post-judgment interest, concerns the quantum and thus the adequacy of that remuneration ...

12 In agreement with the judge and the Court of Appeal, I do not accept the bank’s submission on this issue. The regulations, as Professor Sir Guenter Treitel QC has aptly observed (The Law of Contract, 10th ed, 1999, p 248) ‘are not intended to operate as a mechanism of quality or price control’ and regulation 3(2) is of ‘crucial importance in recognising the parties’ freedom of contract with respect to the essential features of their bargain’ (ibid, at p 249). But there is an important ‘distinction between the term or terms which express the substance of the bargain and “incidental” (if important) terms which surround them’ (Chitty on Contracts, 28th ed, 1999, ‘Unfair Terms in Consumer Contracts’, p 747, para 15-025). The object of the regulations and the directive is to protect consumers against the inclusion of unfair and prejudicial terms in standard-form contracts into which they enter, and that object would plainly be frustrated if regulation 3(2)(b) were so broadly interpreted as to cover any terms other than those falling squarely within it. In my opinion the term, as part of a provision prescribing the consequences of default, plainly does not fall within it. It does not concern the adequacy of the interest earned by the bank as its remuneration but is designed to ensure that the bank’s entitlement to interest does not come to an end on the entry of judgment. I do not think the bank’s argument on merger advances its case. It appears that some judges in the past have been readier than I would be to infer that a borrower’s covenant to pay interest was not intended to extend beyond the entry of judgment. But even if a borrower’s obligation were ordinarily understood to extend beyond judgment even in the absence of an independent covenant, it would not alter my view of the term as an ancillary provision and not one concerned with the adequacy of the bank’s remuneration as against the services supplied. It is therefore necessary to address the second question.

(2) Unfairness

[Lord Bingham set out the test of unfairness in the then reg. 4 of the 1994 Regulations, later regs. 5 and 6 and Sch. 2 of the 1999 Regulations and now s. 62(4) and (5), s. 63(1), and Sch. 2, Part 1 CRA 2015, set out at pages 334-6, section 7.5.3.]

17 The test laid down by regulation 4(1), deriving as it does from article 3(1) of the directive, has understandably attracted much discussion in academic and professional circles and helpful submissions were made to the House on it. It is plain from the recitals to the directive that one of its objectives was partially to harmonise the law in this important field among all member states of the European Union. (p. 338) The member
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states have no common concept of fairness or good faith, and the directive does not purport to state the law of any single member state. It lays down a test to be applied, whatever their pre-existing law, by all member states. If the meaning of the test were doubtful, or vulnerable to the possibility of differing interpretations in differing member states, it might be desirable or necessary to seek a ruling from the European Court of Justice on its interpretation. But the language used in expressing the test, so far as applicable in this case, is in my opinion clear and not reasonably capable of differing interpretations. A term falling within the scope of the regulations is unfair if it causes a significant imbalance in the parties’ rights and obligations under the contract to the detriment of the consumer in a manner or to an extent which is contrary to the requirement of good faith. The requirement of significant imbalance is met if a term is so weighted in favour of the supplier as to tilt the parties’ rights and obligations under the contract significantly in his favour. This may be by the granting to the supplier of a beneficial option or discretion or power, or by the imposing on the consumer of a disadvantageous burden or risk or duty. The illustrative terms set out in Schedule 3 to the regulations provide very good examples of terms which may be regarded as unfair; whether a given term is or is not to be so regarded depends on whether it causes a significant imbalance in the parties’ rights and obligations under the contract. This involves looking at the contract as a whole. But the imbalance must be to the detriment of the consumer; a significant imbalance to the detriment of the supplier, assumed to be the stronger party, is not a mischief which the regulations seek to address. The requirement of good faith in this context is one of fair and open dealing. Openness requires that the terms should be expressed fully, clearly and legibly, containing no concealed pitfalls or traps. Appropriate prominence should be given to terms which might operate disadvantageously to the customer. Fair dealing requires that a supplier should not, whether deliberately or unconsciously, take advantage of the consumer’s necessity, indigence, lack of experience, unfamiliarity with the subject matter of the contract, weak bargaining position or any other factor listed in or analogous to those listed in Schedule 2 of the regulations. Good faith in this context is not an artificial or technical concept; nor, since Lord Mansfield was its champion, is it a concept wholly unfamiliar to British lawyers. It looks to good standards of commercial morality and practice. Regulation 4(1) lays down a composite test, covering both the making and the substance of the contract, and must be applied bearing
clearly in mind the objective which the regulations are designed to promote …

20 In judging the fairness of the term it is necessary to consider the position of typical parties when the contract is made. The borrower wants to borrow a sum of money, often quite a modest sum, often for purposes of improving his home. He discloses an income sufficient to finance repayment by instalments over the contract term. If he cannot do that, the bank will be unwilling to lend. The essential bargain is that the bank will make funds available to the borrower which the borrower will repay, over a period, with interest. Neither party could suppose that the bank would willingly forgo any part of its principal or interest. If the bank thought that outcome at all likely, it would not lend. If there were any room for doubt about the borrower’s obligation to repay the principal in full with interest, that obligation is very clearly and unambiguously expressed in the conditions of contract. There is nothing unbalanced or detrimental to the consumer in that obligation; the absence of such a term would unbalance the contract to the detriment of the lender …

LORD STEYN: 36 … It is now necessary to refer to the provisions which prescribe how it should be determined whether a term is unfair. Implementing article 3(1) of the directive regulation 4(1) provides:

‘unfair term’ means any term which contrary to the requirement of good faith causes a significant imbalance in the parties’ rights and obligations under the contract to the detriment of the consumer.

There are three independent requirements. But the element of detriment to the consumer may not add much. But it serves to make clear that the directive is aimed at significant imbalance against the (p. 339) consumer, rather than the seller or supplier. The twin requirements of good faith and significant imbalance will in practice be determinative. Schedule 2 to the Regulations, which explains the concept of good faith, provides that regard must be had, amongst other things, to the extent to which the seller or supplier has dealt fairly and equitably with the consumer. It is an objective criterion. Good faith imports, as Lord Bingham has observed in his opinion, the notion of open and fair dealing: see also Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd [1989] QB 433. And helpfully the commentary to the 2000 edition of Principles of European Contract Law, prepared by the Commission of European Contract Law, explains that the purpose of the provision of good faith and fair dealing is ‘to enforce community standards of
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fairness and reasonableness in commercial transactions’: at 113; A fortiori that is true of consumer transactions. Schedule 3 to the Regulations (which corresponds to the Annex to the directive) is best regarded as a check list of terms which must be regarded as potentially vulnerable. The examples given in Schedule 3 convincingly demonstrate that the argument of the bank that good faith is predominantly concerned with procedural defects in negotiating procedures cannot be sustained. Any purely procedural or even predominantly procedural interpretation of the requirement of good faith must be rejected.

37. That brings me to the element of significant imbalance. It has been pointed out by Hugh Collins that the test ‘of a significant imbalance of the obligations obviously directs attention to the substantive unfairness of the contract’: ‘Good Faith in European Contract Law,’ (1994), 14 Oxford Journal of Legal Studies 229, 249. It is however, also right to say that there is a large area of overlap between the concepts of good faith and significant imbalance.

38. It is now necessary to turn to the application of these requirements to the facts of the present case. The point is a relatively narrow one. I agree that the starting point is that a lender ought to be able to recover interest at the contractual rate until the date of payment, and this applies both before and after judgment. On the other hand, counsel for the Director advanced a contrary argument. Adopting the test of asking what the position of a consumer is in the contract under consideration with or without clause 8, he said that the consumer is in a significantly worse position than he would have been if there had been no such provision. Certainly, the consumer is worse off. The difficulty facing counsel, however, is that this disadvantage to the consumer appears to be the consequence not of clause 8 but of the County Courts (Interest on Judgment Debts) Order 1991. Under this Order no statutory interest is payable on a county court judgment given in proceedings to recover money due under a regulated agreement: see regulation 2. Counsel said that for policy reasons it was decided that in such a case no interest may be recovered after judgment. He said that it is not open to the House to criticise directly or indirectly this legal context. In these circumstances he submitted that it is not legitimate for a court to conclude that fairness requires that a lender must be able to insist on a stipulation designed to avoid the statutory regime under the 1991 Order. Initially I was inclined to uphold this policy argument. On reflection, however, I have been persuaded that this argument cannot prevail in circumstances where the legislature has neither expressly nor by necessary
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implication barred a stipulation that interest may continue to accrue after judgment until payment in full.

39. For these reasons as well as the reasons given by Lord Bingham I agree that clause 8 is not unfair . . .

Notes

1. ‘Significant imbalance’ imports considerations of the substantive fairness of the term judged in the context of the contract terms as a whole.

2. Professor Beale, ‘Legislative control of fairness: The Directive on Unfair Terms in Consumer Contracts’, in Beaton and Friedmann (eds.), Good Faith and Fault in Contract Law (Oxford University Press, 1995), p. 245, regarded good faith as having a dual operation—namely, the procedural aspects of good faith (preventing unfair surprise) and the substantive aspect concerning any imbalance in the content of the clause to the detriment of the consumer. Their Lordships clearly accepted that ‘significant imbalance’ is substantive, but appeared to consider (p. 340) that ‘good faith’ refers to both procedural and substantive unfairness. Lord Bingham identified ‘good faith’ as a requirement of ‘fair and open dealing’. Whereas ‘openness’ clearly refers to procedural matters, ‘fairness’ can encompass both substantive and procedural matters, and Lord Bingham’s examples refer to issues of unconscionability such as taking advantage of a weakness in bargaining position. Lord Steyn commented, at [37], that ‘there is a large area of overlap between the concepts of good faith and significant imbalance’, which also suggests that he saw good faith as involving substantive fairness.

3. The House of Lords was prepared to accept on these facts that the position for consumers was unsatisfactory. However, any unfairness did not result from the term in question, but from the inability of the county court to take account of contractual interest when giving judgment on a debt. This has since been amended via the Consumer Credit Act 2006.

4. This decision relates to the 1994 Regulations, but the language of the provisions was also largely reflected in the 1999 Regulations and also, as regards the test of fairness, in Part 2 of the CRA 2015. The exception is the reference in Lord Bingham’s speech to Sch. 2 to the 1994 Regulations, which resembled Sch. 2 to UCTA 1977. There was no equivalent provision in the 1999 Regulations and no such provision is included in the CRA 2015.

5. The statutory provision covering ‘core terms’ is rather different to its predecessors (see s. 64 CRA 2015, pages 335–6)
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in that it is made clear that the Sch. 2 terms can never be ‘core terms’. Neither can any term which specifies the main subject matter of the contract or if the assessment would involve assessing the appropriateness of the price amount, assuming that the term is transparent and prominent. If it is not, then even these terms are subject to the s. 62 fairness test.

6. Spreadex Ltd v Cochrane [2012] EWHC 1290 (Comm) shows an application of both substantive and procedural unfairness. The clause in question resulted in the consumer having potential unlimited liability in all circumstances for any unauthorized dealings with its online spread betting account with the bookmaker, e.g. even if the consumer was able to demonstrate that he had not been negligent. The judge also considered that the manner for giving notice of this clause was inadequate, i.e. the consumer was told that four documents could be viewed elsewhere by clicking on a key. The customer agreement containing the clause was in small print and extended for 49 pages. It was considered most unlikely that it would have been read.

7. In West v Ian Finlay & Associates [2014] EWCA Civ 316, [2014] BLR 324, the Court of Appeal had to consider the fairness of a ‘net contribution clause’ in a contract with a firm of architects to renovate a domestic house. A Net Contribution Clause (NCC) limits a contractor’s liability to losses for which it is responsible with the aim of avoiding a contractor being liable for losses caused by others (and in the absence of such a clause all wrongdoers would be jointly and severally liable for all loss suffered irrespective of fault). The particular NCC provided that: ‘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.’ The main contractor was insolvent and the householders sued the architects, who were responsible for coordinating the work done by a series of contractors, seeking damages in respect of defective renovations. The architects argued that their liability was limited by the NCC because the main contractor had also been at fault.

The Court of Appeal held that such clauses could be fair if drafted in clear terms. Although the NCC clearly resulted in an imbalance in the parties’ rights and obligations because it limited the householders’ ability to recover in full against the architects, this was not ‘significant’ because net contribution clauses are standard in industry forms. In any event, the clause was not contrary to good faith since it had been clearly presented and did not represent a concealed trap, the householders were perfectly able to understand the NCC, and the parties were of broadly equal bargaining power. Moreover, it was not necessarily unfair to seek to exclude responsibility for
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the wrongs of others and the householder could take out insurance to cover the risks of any insolvency by a contractor.

7.5.4.2 Terms excluded from the assessment of fairness: so-called ‘core terms’

Under the UTCCR 1999 if the terms were excluded from the scope of the Regulations as ‘core terms’ by reg. 6(2) they could not be assessed for unfairness. The courts sometimes sought to avoid this conclusion as part of a protectionist approach by holding that reg. 6(2) (‘core terms’) was to be interpreted restrictively, so allowing more terms to be assessed for unfairness.

(p. 341) Bairstow Eves London Central Ltd v Smith


A term in an estate agency contract provided for commission at the rate of 1.5 per cent if paid in full within ten days of completion or agreed alternative payment date; otherwise, commission was payable at 3 per cent on the sale price with interest at 3 per cent above base. The judge had concluded that this was not a ‘core term’ (i.e. did not concern the adequacy of the price or remuneration), and that the 3 per cent term was unfair and so not binding on the vendors. The estate agents appealed on the applicability of the Regulations.

**Held:** The issue here was whether the core rate was 3 per cent with an option to pay 1.5 per cent (in which case, reg. 6(2) was applicable) or whether the core rate was 1.5 per cent with a ‘default’ provision of 3 per cent. The judge concluded that the 1.5 per cent was contemplated as the price, with a default position of 3 per cent if the vendors failed to pay within ten days. Accordingly, reg. 6(2) did not apply and the Regulations as a whole were applicable. The issue of unfairness was not appealed.

Relying on the guidance in *Director General of Fair Trading v First National Bank*, the judge concluded as follows.

GROSS J: 25 ... Guided by this authority, the landscape becomes clear. The object of the Regulations is not price control nor are the Regulations intended to interfere with the parties’ freedom of contract as to the essential features of their bargain. But, that said, regulation 6(2) must be given a restrictive interpretation; otherwise a coach and horses could be driven through the Regulations. So, while it is not for the Court to rewrite the parties’ bargain as to the fairness or adequacy of the
price itself, regulation 6(2) may be unlikely to shield terms as to price escalation or default provisions from scrutiny under the fairness requirement contained in regulation 5(1). I say ‘may be unlikely’ because, of course, much depends on the individual contract under consideration. When, however, regulation 6(2) is inapplicable so that regulation 5(1) is engaged, it does not follow that a term will be adjudged unfair; whether or not a term is unfair involves a separate inquiry but one which cannot be undertaken at all insofar as regulation 6(2) is applicable and bars the way.

Notes

1. Although the judge is clear that ‘much depends on the individual contract under consideration’, the approach to assessing whether a term fell within reg. 6(2) must now be read in the light of the approach taken by the Supreme Court in Office of Fair Trading v Abbey National plc [2009] UKSC 6, [2010] 1 AC 696. On the facts, terms relating to bank charges were held to fall within reg. 6(2) on the plain meaning of the words in that regulation, so construction may be more important than policy. 2. In Baybut v Eccle Riggs Country Park Ltd (2006) The Times, 13 November, an express term providing for a yearly licence to use a static caravan park was held to be ‘a core term’ within reg. 6(2) as defining the main subject matter of the contract. Moreover, although the UTCCR 1999 are not expressly limited to express terms, the judge considered it ‘highly unlikely’ that they were intended to have any application to implied terms. Terms implied by the courts at common law can be implied only if reasonable, so that the judge considered they could not then be found to be ‘unfair’.

7.5.4.2.1 The bank charges litigation

The scope of reg. 6(2) UTCCR 1999 was at issue in the ‘bank charges’ litigation, in which the banks alleged that the terms imposing such charges could not be assessed for unfairness since they were ‘core terms’ within the then reg. 6(2)(b), i.e. the terms imposing charges related to the adequacy of the price or remuneration, as against the goods or services supplied in exchange. (Banking is generally free for those customers who stay in credit, but fixed fees and interest are payable by customers with overdrafts—particularly customers who have unauthorized overdrafts.) The Court of Appeal concluded that the bank charges were ‘ancillary’ and so not part of ‘the core terms’ of the contract.

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to which reg. 6(2)(b) applied. However, the Supreme Court reversed this, accepting the argument of the banks that the bank charges were part of the ‘core bargain’ and fell within reg. 6(2)(b) as being ‘the price or remuneration, as against the service supplied in exchange’.

Office of Fair Trading v Abbey National plc


LORD WALKER OF GESTINGTHORPE JSC: 40 ... [A] supply of services may be simple (an entertainer booked to perform for an hour at a children’s party) or composite (a week’s stay at a five-star hotel offering a wide variety of services) ... [T]here is no principled basis on which the court could decide that some services are more essential to the contract than others and ... the main subject matter must be described in general terms—hotel services. The services that banks offer to their current account customers are a comparable package of services. These include the collection and payment of cheques, other money transmission services, facilities for cash distribution (mainly by ATM machines either at manned branches or elsewhere) and the provision of statements in printed or electronic form.

41 When one turns to the other part of the quid pro quo of a consumer contract, the price or remuneration, the difficulty of deciding which prices are essential is just the same, and regulation 6(2)(b) contains no indication that only an ‘essential’ price or remuneration is relevant. Any monetary price or remuneration payable under the contract would naturally fall within the language of paragraph (b) (I discount the absence of a reference to part of the price or remuneration ...).

42 In the case of banking services supplied to a current account customer under the ‘free-if-in-credit’ regime, the principal monetary consideration received by the bank consists of interest and charges on authorised and unauthorised overdrafts, and specific charges for particular non-routine services (such as expedited or foreign money transmission services). The most important element of the consideration, however, consists of the interest foregone by customers whose current accounts are in credit, since whether their credit balance is large or small, they will be receiving a relatively low rate of interest on it (sometimes a very low rate or no interest at all) ... [Counsel] was wary about committing himself as to whether interest foregone constituted part of the bank’s price or remuneration for the purposes of regulation 6(2)(b). Whatever view is taken as to that, it is clear that just as banking
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services to current account customers can aptly be described as a package, so can the consideration that moves from the customer to the bank. Interest foregone is an important part of that package for customers whose accounts are in credit, and overdraft interest and charges are the most important element for those customers who are not in credit. Lawyers are very used to speaking of a package (or bundle) of rights and obligations, and in that sense every obligation which a consumer undertakes by a consumer contract could be seen as part of the price or remuneration received by the supplier. But non-monetary obligations undertaken by a consumer contract (for instance, to take proper care of goods on hire-purchase, or to treat material supplied for a distance-learning course as available only to the customer personally) are not part of the ‘price or remuneration’ within the regulation. That is the point of Lord Steyn’s observation in the First National Bank case [2002] 1 AC 481, para 34, that ‘in a broad sense all terms of the contract are in some way related to the price or remuneration’.

(p. 343)

43 The House of Lords’ decision in the First National Bank case shows that not every term that is in some way linked to monetary consideration falls within regulation 6(2)(b). Paragraphs (d), (e), (f) and (l) of the ‘greylist’ in Schedule 2 to the 1999 Regulations are an illustration of that. But the relevant term in the First National Bank case was a default provision. Traders ought not to be able to outflank consumers by ‘drafting themselves’ into a position where they can take advantage of a default provision. But Bairstow Eves London Central Ltd v Smith [2004] 2 EGLR 25 shows that the court can and will be astute to prevent that. In the First National Bank case Lord Steyn, at para 34, indicated that what is now regulation 6(2) should be construed restrictively, and Lord Bingham said, at para 12, that it should be limited to terms ‘falling squarely within it’. I respectfully agree. But in my opinion the relevant terms and the relevant charges do fall squarely within regulation 6(2)(b) ...

The application of regulation 6(2)

47 ... Charges for unauthorised overdrafts are monetary consideration for the package of banking services supplied to personal current account customers. They are an important part of the banks’ charging structure, amounting to over 30% of their revenue stream from all personal current account customers. The facts that the charges are contingent, and that the majority of customers do not incur them, are irrelevant. On the view that I take of the construction of regulation 6(2), the fairness of the charges would be exempt from review in point of appropriateness under regulation 6(2)(b) even if fewer
customers paid them, and they formed a smaller part of the banks’ revenue stream. Even if the Court of Appeal’s interpretation had been correct, I do not see how it could have come to the conclusion [2009] 2 WLR 1286, para 111 that charges amounting to over 30% of the revenue stream were ‘not part of the core or essential bargain’ …

Conclusion

51 For these reasons I would allow the appeal … I would declare that the bank charges levied on personal current account customers in respect of unauthorised overdrafts (including unpaid item charges and other related charges) constitute part of the price or remuneration for the banking services provided and, in so far as the terms giving rise to the charges are in plain intelligible language, no assessment under the Unfair Terms in Consumer Contracts Regulations 1999 of the fairness of those terms may relate to their adequacy as against the services supplied.

Notes

1. The Supreme Court rejected the distinction between sums that represented the core bargain and ancillary sums. There was no principled basis for treating some terms as more essential than others in this context. The Court of Appeal in the ‘bank charges’ case—Office of Fair Trading v Abbey National plc [2009] EWCA Civ 116, [2009] 2 WLR 1286—and Mann J in Office of Fair Trading v Foxtons Ltd [2009] EWHC 1681(Ch), [2009] EGLR 133, [2009] EG 98 (CS), had placed great reliance on this distinction and on the perceptions of customers concerning the nature of the respective charges. In the Foxtons case, the issue was whether renewal commissions were part of a single category of ‘commission payment’ and so part of the ‘price’ for the service.

2. In Abbey National the question was only whether the charges represented the monetary price for the service provided in exchange under the contract. Not all terms would fall within this definition—First National Bank and Bairstow Eves were cited as examples—but these charges clearly did. They were part of the customer’s package and the price paid for banking services.

3. Although it was expressly rejected by the Court of Appeal and by Mann J in the Foxtons case, the Supreme Court settled on a construction approach to whether terms fell within reg. 6(2), rather than an approach that tried to assess how the term was perceived by customers, including reasonable expectations, and
4. In *Office of Fair Trading v Ashbourne Management Services Ltd* [2011] EWHC 1237 (Ch), [2011] ECC 31, the court had to consider whether terms setting minimum membership periods of between 12 and 36 months in contracts for gym membership were core terms within reg. 6(2), or ancillary and so capable of being assessed under the Regulations. Although it might be thought that the main subject of such an agreement is the membership and right to use the club, and that the period of time for which this applied would be ancillary to this, the judge held that the period of membership was a core term. However, since reg. 6(2)(b) precluded the assessment of fairness only by reference to the adequacy of the price or remuneration as against the services supplied, the judge thought that reg. 6(2)(a) should also preclude an assessment for fairness only by reference to the definition of the main subject matter. It was therefore possible to assess this clause for fairness pertaining to the consequences for members of early termination of their memberships.

Some of the minimum periods were weighted to cause a significant imbalance in the parties’ respective positions, which was contrary to good faith. These periods were designed to exploit consumer’s overestimation of their use of their gym membership.

KITCHIN J:

*Does the term imposing a minimum membership period fall within the scope of regulation 6(2)(a) UTCCR?*

152 Turning now to the application of these principles in the context of this case, I believe that the main subject matter of each of Ashbourne’s standard form agreements involves, on the one hand, the agreement by the gym club that a consumer may become a member of the club and use and access its facilities for the minimum period and, on other hand, the payment by the member of a monthly subscription of a certain sum, again for that minimum period. I do not accept that a term providing for the minimum period is not a ‘core term’ but is merely a ‘subsidiary provision’, as the OFT urged upon me. There is a danger in using these expressions as shorthand for the words of reg. 6(2) as the Supreme Court explained in the *Abbey National* case. However, in so far as it is helpful to use them, I believe that cl. 2 of each of the agreements is a core term rather than a subsidiary provision because it defines the period during which the member is entitled to use the facilities of the gym club and, in return, must pay a
particular monthly subscription. Nor do I believe the OFT gains any assistance from paras 1(b), (e) or (o) of the indicative list of terms. These all concern terms dealing in one way or another with default or non-performance. I therefore believe that cl. 2 of each of the agreements does fall within the scope of reg. 6(2).

153 That is not the end of the analysis, however, because the question then arises as to whether reg. 6(2)(a) precludes any assessment of the fairness of cl. 2 of each of the agreements or whether the regulation only precludes an assessment relating to the definition of the main subject matter of the contract, that is to say its meaning, description and clarity. In the Abbey National case the Supreme Court was, of course, only concerned with the scope of para. (b) of reg. 6(2). Nevertheless, it seems to me that there is no basis for drawing a distinction between the two paragraphs in this regard. If reg. 6(2)(b) only precludes the assessment of the fairness of a term by reference to the adequacy of the price or remuneration as against the goods or services supplied then, in my judgment, it follows that reg. 6(2)(a) only precludes the assessment of the fairness of a term by reference to the definition of the main subject matter of the contract. This is not only the natural meaning of the words used in reg. 6(2) but also gives effect to the purpose of its two paragraphs as explained by Lord Walker JSC. Moreover, as the House of Lords explained in the First National Bank case, this regulation should be given no wider an interpretation than necessary ...

**Fairness**

173 In all these circumstances I believe that the defendants’ business model is designed and calculated to take advantage of the naivety and inexperience of the average consumer using gym clubs at the lower end of the market. As the many complaints received by the OFT show, the defendants’ standard form agreements contain a trap into which the average consumer is likely to fall.

174 I must of course give weight to the requirement that there must be a *significant* imbalance. Taking this and all the other matters to which I have referred into account I have reached the conclusion that the terms of agreements 1–10 setting minimum membership periods of 12, 24 or 36 months are so weighted as to cause a significant imbalance in the parties’ rights and obligations in a manner and to an extent which is contrary to good faith. The position in relation to agreements 11–13 is, I believe, different because they do extend the circumstances in which members may terminate before the end of the
minimum period. In the case of these agreements I have come to the conclusion that the threshold is higher and that a significant imbalance in the parties’ rights and obligations in a manner or to an extent which is contrary to good faith only arises in those cases in which the minimum term exceeds 12 months, that is to say those which provide for a minimum membership period of 24 or 36 months. My conclusion in relation to these later agreements might well have been different had they permitted the member to terminate after 12 months on, say, 30 days’ notice, perhaps with a provision requiring the member to pay the difference between the agreed subscription and that for a rolling monthly membership for the period prior to the date of termination.

This brings me to the final part of the analysis, namely whether this assessment of fairness relates to the definition of the main subject matter of the agreements. In my judgment it does not. The assessment does not relate to the meaning or description of the length of the minimum period, the facilities to which the member gains access or the monthly subscription which he has to pay; nor does it relate to the adequacy of the price as against the facilities provided. Instead it relates to the obligation upon members to pay monthly subscriptions for the minimum period when they have overestimated the use they will make of their memberships and failed to appreciate that unforeseen circumstances may make their continued use of a gym impractical or their memberships unaffordable. Put another way, it relates to the consequences to members of early termination in light of the minimum membership period. Accordingly I believe the assessment is not precluded by reg. 6(2).

The wording of s. 64 CRA 2015 (see pages 335–6) is seemingly designed to eliminate any need for ‘ancillary’ terms by clearly indicating that the only ‘core terms’ are those that ‘specify the main subject matter of the contract’ or relate to the amount of the price paid for the goods or services. Even these core terms must be transparent and prominent or they will fall within the scope of the test for fairness.