

Risk Bulletin

Managing Contractual Liability

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Risk management is often focused on critical areas such as property protection and worker safety. An equally important area is contractual liability. A properly written and reviewed contract can help to mitigate the cost of a claim and perhaps prevent your client's company from paying unnecessarily for disputes and claims that may be more the responsibility of third parties, subcontractors, or others.

The practical tips set forth below address contractual liability. As with any legal matter, you should consult with your own legal counsel prior to entering into any contract.

Contracts and Agreements

Legal review - Have your legal counsel review and approve all standard contracts, purchase orders, as well as license and service agreements, including those with subcontractors.

Customising contracts - To the greatest extent possible, it is better to avoid customising contracts. If an agreement must be customised, use boilerplate amendments that become "standard exceptions," or make sure your legal counsel reviews all deviations from standard.

Limitations of liability - Where possible, take advantage of all contract language measures that enable limited liability and tailor the language to a specific industry. In doing so, all consequential, punitive and similar

damages can effectively be limited to the cost of the contract or service provided.

Disclaiming warranties - Warranty disclaimers may be inserted in contracts. They help minimise exposure to litigation by limiting the types of warranties that parties are willing to offer. These disclaimers should conform to local jurisdictional requirements and, for US-related contracts, the requirements of the Uniform Commercial Code with regard to typestyle and content.

Warranties - Some warranties are difficult to meet. Making the warranties as specific as possible, and avoiding the use of "general warranties" wherever possible, would be a more sensible approach.

Severability - Including a severability clause allows the parties to rely on provisions that limit liability and may be jeopardised if a court finds another provision of the contract unenforceable.

Indemnities - Having indemnification wording to the benefit of one party can insure that party's assets are covered.

Arbitration - Including arbitration provisions in contracts provides a way to resolve customer disputes in lieu of litigation.

Force majeure - This wording is important for all companies, but is especially critical for technology companies and businesses that rely on communications infrastructure to deliver services or products to its

customers. Force majeure clauses may limit liability for losses or breaches resulting from external forces such as earthquakes, tornados, storms or other natural events, as well as events such as war. Rather than relying on a blanket clause stating “anything outside of your control”, it is useful to specifically list these things.

Performance specifications - When negotiating contracts, it is a good idea to ensure that all parties agree to the specific expectations, promises and contingencies regarding the performance of the contract. Complete RFPs (Requests for Proposal) and contract performance obligations should be included, as well as confirming whether or not critical employees are expected to be present throughout the course of the contract. If third parties are involved with a project, the customer should know exactly what you are and are not providing. Likewise, you should have confidence in the systems you are using, acquiring or recommending. Contracts should be specific regarding agreed-upon definitions, performance specifications, timetables, dealing with changes and the processes and procedures to be used in dispute resolution.

Performance obligations - It’s best to be specific but brief with regard to performance obligations. Brevity will create much more clarity around this issue.

Amendments and modifications - Specify the procedures for making amendments and modifications to your contract. It’s a good idea to document any changes made to product and service specifications and deliverables.

Contract length - If possible, implement smaller projects under multiple short term contracts. Longer contracts tend to be more complex and may change over time, presenting more opportunities for missed completion dates, which can lead to litigation resulting from failure

or non-delivery of a project. If shorter-term contracts are not an option, a company could conduct a thorough risk assessment of the entire project. Consider such factors as the scope and inherent feasibility of the project, stability of customer requirements, development and quality practices of the manufacturers, and how realistic the time and resource estimates needed to successfully complete the project are. Include Statements of Work (SOW) or other milestone documentation requirements to track and measure a project’s progress.

Operational Controls

Legal review of advertising materials and product brochures It’s good practice for legal counsel to review all advertising and marketing materials with regard to the promises explicitly made or implied to customers. It’s best to set realistic expectations and avoid absolutes in marketing materials. Product and promotional literature may inadvertently communicate expressed or implied warranties not contemplated in the contracts that are being used.

Accounts receivable collection procedures - Be cautious when changing your accounts receivable collection procedures. Changing such practices may lead to customer disputes.

Sales and marketing training - Seek legal counsel’s assistance in developing sales and marketing training programs that control product oversell and puffery. If any confusion exists between what a salesperson tells a customer and what the contract says, a claim may be made for misrepresentation or fraudulent inducement.

Certificates of insurance - There is the option to require subcontractors and vendors supplying or doing work to name a company as an additional insured on their insurance policies,

including Errors & Omissions. A company could obtain certificates of insurance from all vendors and subcontractors as evidence that they have complied with your requirement and maintain a file containing these certificates. The certificates should specify effective dates, limits and coverage afforded and updated certificates should be obtained on an annual basis for the duration of the working relationship.

Disputes and Allegations of Non-performance

Loss history - A thorough loss history can be a window on future litigation problems and can be used to help identify and eliminate potential sources of loss, claims, and litigation by carefully analysing all non-performance issues, claims and litigation as well as their causes - including all suits, potential suits, complaint letters, disputes, or any other circumstances alleging non-performance of products or services.

Product rollbacks or recalls - If there have been product rollbacks or recalls in the past, it may be useful to document why they occurred and the remedies used for resolving customer loss of use.

Contract delays - By examining the causes of any contract delays experienced, it may be determined if the delays arose from promising unrealistic deadlines or agreeing to unrealistic customer expectations. The issue can then be addressed with sales force and customers and more reasonable contract terms can be negotiated.

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