

## Construction Law Update

### Court of Appeal finds that Limitation of Liability Clause does not Exclude a Claim for Wasted Expenditure

In *Soteria Insurance Ltd v IBM United Kingdom Ltd* [2022], the Court of Appeal overturned a High Court decision by finding that the words “loss of profit, revenue, savings (including anticipated savings)” in a limitation of liability clause did not exclude a claim for wasted expenditure.

#### Background

On 16 June 2015, Cis General Insurance Limited (“**CISGIL**”) (latterly Soteria Insurance Limited), entered into a written contract with IBM United Kingdom Limited (“**IBM**”) for the supply, installation and management of an IT system (the “**Contract**”) for a sum of £175.8million.

A series of delays, for which IBM was responsible, ultimately meant that the IT system was never delivered. A dispute arose following non-payment of a milestone invoice (the “**Invoice**”), following which, IBM terminated the Contract.

CISGIL commenced proceedings against IBM on the basis that IBM had wrongfully repudiated the Contract and sought damages for wasted expenditure flowing from the repudiation in the sum of £132 million. CISGIL also claimed for IBM’s alleged breach of warranty and delay under the Contract. IBM defended the claims on the basis that non-payment of the Invoice entitled it to terminate the Contract. IBM also counterclaimed £2.9million for the sum due under the Invoice.

At first instance, the High Court found that:

- (a) IBM had wrongfully repudiated the Contract;
- (b) CISGIL had in principle established a claim valued at £122million for wasted expenditure following IBM’s repudiation;
- (c) CISGIL’s claim for wasted expenditure was nevertheless excluded by an exclusion clause in the Contract (the “**Exclusion Clause**”);

- (d) CISGIL was entitled recover £15,887,990 in damages for additional costs and losses following IBM’s other breaches;
- (e) IBM was entitled to set-off against the value of the Invoice (£2.9million); and
- (f) CISGIL was entitled to recover damages in the net sum of £12,998,390 together with interest.

This bulletin concerns CISGIL’s subsequent appeal against limb (c) of the High Court’s decision (the “**Appeal**”) concerning the proper construction of the Exclusion Clause.

IBM cross-appealed against the finding that it had wrongfully repudiated the Contract and contended that CISGIL’s wasted expenditure was attributable to a change in its strategic direction rather than termination of the Contract (the “**Cross-Appeal**”).

#### Held

The Appeal was allowed and the Cross-Appeal was dismissed.

#### Construction of the Exclusion Clause

The Court of Appeal found that the judge was wrong to construe the Exclusion Clause as precluding CISGIL from recovering wasted expenditure following IBM’s repudiation of the Contract, albeit the existence of a contractual cap meant that recovery was limited to c.£80.5million in this regard.

Citing several well-known authorities, the Court explained that in determining what losses were excluded from recovery under the Contract, the starting point was to give the words making up the Exclusion Clause their natural and ordinary meaning. The first instance judge had failed to engage with this exercise.

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The Contract defined “losses” widely and carved out specific types of loss that would be excluded which included “loss of profit, revenue [or] savings”. The term “wasted expenditure”, however, was not referred to in the Contract. On this analysis, the Exclusion Clause, as understood by a reasonable person in the position of the parties did not exclude a claim for wasted expenditure and the words “loss of profit, revenue [or] savings” were incapable of encapsulating the same.

The Court also reasoned that the more valuable the right which one party seeks to exclude, the clearer the language of any exclusion clause will need to be. With this in mind, the Exclusion Clause did not contain the necessary clear wording to exclude liability for costs incurred (and subsequently wasted) following IBM’s repudiation of the Contract. Wasted expenditure was an obvious and common type of loss and the parties could not be taken to have excluded this in the absence of any express reference to the same.

The Court also found that it made commercial sense for consequential losses (such as loss of profits, revenue and savings), which are notoriously open-ended and difficult to ascertain to be excluded but for a different type and more easily ascertainable type of loss (such as wasted expenditure) not to be.

### Repudiation

The Court also found that the judge had been entitled to find that CISGIL had validly disputed the Invoice in good faith and that IBM was not entitled to rely on the non-payment of the Invoice to justify termination of the Contract. Reasons cited in support of this included:

- Contrary to IBM’s suggestion that CISGIL had not disputed the Invoice because it had not used the word “dispute” and / or triggered the dispute machinery in the Contract, the Court found that the Invoice had been validly disputed. A common-sense approach to the meaning of “dispute” dictated that CISGIL had notified IBM of the Invoice dispute by expressly stating in an email that it could not “accept

[the Invoice] for payment” and that was sufficient (*Mannai Investment* followed).

- CISGIL had acted fairly and honestly and had not acted in a commercially unacceptable way to frustrate the purpose of the Contract and IBM had not been given permission to re-open those findings.
- The recipient of the Invoice, a person in CISGIL’s accounts department, simply did their job by notifying IBM that the Invoice could not be accepted because it did not contain information required under the Contract.
- The prevention principle (which provides that a contract should not be construed to enable a contract-breaker to take advantage of their own breach) did not apply.

### Set Off

Although a purely academic consideration in view of the Court’s findings above, the Court also found the judge was correct in finding that CISGIL could not rely on equitable set-off as a reason for withholding payment under the Invoice. The Contract set out a clear mechanism governing CISGIL’s ability to rely on equitable set-off and this had not been complied with following receipt of the Invoice.

### Analysis

This case highlights the importance of accurate and unambiguous drafting where one party seeks to exclude or cap liability for a specific head of loss, which in this case related to wasted expenditure.

This case also suggests that the courts will be more stringent in their interpretation of exclusion clauses where parties have been more specific about the types of loss they intend to exclude.

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