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Waiving the Right to Get Paid

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A recent case in Nassau County highlights the risks of limitation of liability clauses.

The most important document determining a construction contractor's legal rights and remedies is its contract. The law gives contracting parties tremendous flexibility to craft their contract as they see fit and, generally, the courts will enforce a mutually-agreed contract according to its terms. However, a recent case in Nassau County highlights that, in doing so, the law also allows parties to waive important legal rights as part of their agreement, including the right to claim certain monetary damages if the contract is breached.

In the case, *R & J Construction Corp. v. E.W. Howell Company, Inc.*, decided in May 2008, the plaintiff, R&J, was a carpentry subcontractor to the defendant, Howell, on the Civil Court refurbishment project in Riverhead. After R&J had completed some of the work called for under its contract, a heated dispute arose between Howell and R&J – including an alleged physical altercation between senior executives of each company – with accusations of delay and failure to perform going back and forth between them. Unable to resolve these disputes, Howell terminated R&J's contract, and R&J sued Howell for approximately \$535,000. Of the \$535,000 that R&J claimed against Howell in its lawsuit, over \$400,000 was for "consequential" damages and lost profits resulting from Howell's alleged wrongful termination of the contract. The balance of the amount claimed was payment for work R&J had already alleged performed at the project.

While the law generally allows contractors to claim "consequential" damages and lost profits

when a contract is improperly terminated, in this case, R&J and Howell had agreed to a "limitation of liability" clause in their contract that specifically barred R&J from claiming these types of damages. The contract stated that Howell could terminate R&J either "for convenience" or "for cause." If Howell terminated R&J "for cause," Howell had the right to claim damages from R&J for Howell's costs to complete the project. On the other hand, if Howell terminated R&J "for convenience," Howell could not claim any damages against R&J. Crucially, however, the contract also stated that, even if the termination was "for convenience," R&J would only be entitled to recover the outstanding balance for work it already performed on the project and it could not claim any other damages from Howell, including lost profits.

Armed with these contractual provisions, in response to R&J's case, Howell argued that the approximately \$400,000 claim for "consequential" damages and lost profits was barred by the contract and should be dismissed from the case. The Court agreed with Howell and dismissed that part of the claim. Specifically, the Court found that even if Howell's termination of the contract had been "for convenience," an issue that had yet to be resolved, the contract still barred R&J from claiming damages above and beyond the amount then due and owing it for work already performed. Therefore, the Court found that the "consequential" damages and lost profits aspect of the claim was barred by the language of the contract regardless of the type of termination – "for cause" or "for convenience." The Court did allow the remaining claim for work performed prior to termination to proceed.

In this case, R&J argued that, even though it



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agreed to the limitation clause in the contract, the clause should not have been enforced because Howell's termination of the contract was intentional and in bad faith. The Court agreed that limitation of liability clauses can be ignored by a court if it finds that the party that terminated the contract "willfully intended to inflict harm" on the other party or otherwise engaged in grossly negligent or intentionally harmful conduct. However, the Court also stated that this was a narrow exception to the general rule that the parties' agreement should be enforced. The Court found that the facts of this case did not support R&J's claim of such conduct by Howell.

It is important to note that the Court based its decision on the specific facts of the case and if R&J could have shown gross negligence or intentionally harmful conduct by Howell in terminating the contract, the result may have been different. However, the important lesson of the case is that signing on to a limitation of liability clause creates a difficult and uphill battle for the right to make a claim that is otherwise allowed under the law. Therefore, contractors should be aware of these clauses and make sure that they understand that they may be compromising important legal rights when they agree to them. <<