

TO THE POINT MANAGING CONTRACTUAL LIABILITY

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 company from paying unnecessarily for disputes and claims that may be more the responsibility of third parties, subcontractors, or others with whom you work.

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 legal counsel review and approve all standard contracts, purchase orders, and license and service agreements, including those with subcontractors.

Customizing contracts — To the greatest extent possible, avoid customizing contracts. If you must customize an agreement, use boilerplate amendments that become “standard exceptions,” or make sure your legal counsel reviews all deviations from standard.

Limitations of liability — Take advantage of all contract language measures that enable you to limit your liability. Tailor this language to your industry and customers. Limit all consequential, punitive and similar damages to ensure that your liability is limited to the cost of the contract or service provided by you.

Disclaiming warranties — Include warranty disclaimers in your contracts. They help minimize your exposure to litigation by limiting the types of warranties that you are willing to offer. These disclaimers should conform to the requirements of the Uniform Commercial Code with regard to typestyle and content, as well as any local jurisdictional requirements.

Warranties — Do not make warranties that are difficult to meet. Make the warranties as specific as possible, avoiding the use of “general warranties” wherever possible.

Severability — Include a severability clause in your contracts. Without it, your ability to rely on provisions in your contract that limit your liability may be jeopardized if a court finds another provision in your contract unenforceable.

Indemnities — Protect your organization’s assets by having indemnification wording that inures to your benefit.

Arbitration — Consider including arbitration provisions in your contracts as a means 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 your 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. Specifically list the things outside of your control rather than relying on a blanket clause stating “anything outside of your control.”

Performance specifications — When negotiating contracts, 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. Confirm whether or not critical employees are expected to be present throughout the course of the contract. If third parties are involved with a project, make sure your customer knows exactly what you are (and are not) providing. Likewise, be sure you 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 — 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. 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, 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. 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 — Ensure that legal counsel reviews all advertising and marketing materials with regard to the promises explicitly made or implied to customers. 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 — Require subcontractors and vendors supplying or doing work for you to name you as an additional insured on their insurance policies, including E&O. 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 — Carefully analyze all non-performance issues, claims and litigation as well as their causes. Include in your review all suits, potential suits, complaint letters, disputes, or any other circumstances alleging non-performance of your products or services. A thorough loss history can be a window on future litigation problems and should be used to help identify and eliminate potential sources of loss, claims, and litigation.

Product rollbacks or recalls — If you have had product rollbacks or recalls in the past, document why they occurred and the remedies used for resolving customer loss of use.

Contract delays — Examine the causes of any contract delays you have experienced. If the delays arose from promising unrealistic deadlines or agreeing to unrealistic customer expectations, address the issue with your sales force and customers and negotiate more reasonable contract terms.

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For more information, contact AmWINS Program Underwriters

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Answer these questions to find out if your company may have contractual exposure. If you answer "No" to any of these questions, you may need assistance developing or enhancing your risk management program to help better protect your company's assets.

Contractual Liability Checklist	Yes	No
Contracts & Agreements		
Does legal counsel review all contracts, orders, and license and service agreements?	<input type="checkbox"/>	<input type="checkbox"/>
Do you always use a standard contract?	<input type="checkbox"/>	<input type="checkbox"/>
Do you limit your liability in all contracts to avoid consequential loss, punitive damages, stipulated damages, or liquidated damages?	<input type="checkbox"/>	<input type="checkbox"/>
Do you include warranties and disclaimers in your contracts and promotional material?	<input type="checkbox"/>	<input type="checkbox"/>
Do all disclaimers and limitations of liability in your contracts conform to applicable requirements in typeface and content?	<input type="checkbox"/>	<input type="checkbox"/>
Are all warranties specific and realistic?	<input type="checkbox"/>	<input type="checkbox"/>
Do your contracts include a severability clause, arbitration clause and "force majeure" wording?	<input type="checkbox"/>	<input type="checkbox"/>
Do your contracts ensure that all parties agree to the specific expectations, promises and contingencies regarding the performance of the contract?	<input type="checkbox"/>	<input type="checkbox"/>
Do you include RFPs and contract performance obligations?	<input type="checkbox"/>	<input type="checkbox"/>
Are your contracts specific regarding definitions, performance specifications and obligations, timetables, dealing with changes and dispute resolution procedures?	<input type="checkbox"/>	<input type="checkbox"/>
Do you confirm whether or not critical employees are expected to be present throughout the course of the contract?	<input type="checkbox"/>	<input type="checkbox"/>
Do you document any changes made to product and service specifications and deliverables?	<input type="checkbox"/>	<input type="checkbox"/>
Do you seek multiple short-term contracts for long projects?	<input type="checkbox"/>	<input type="checkbox"/>
For long-term contracts, do you conduct a risk assessment of the entire project?	<input type="checkbox"/>	<input type="checkbox"/>
For longer-term contracts, do you use Statements of Work (SOW) or other methods of documentation to capture project milestones?	<input type="checkbox"/>	<input type="checkbox"/>
Operational Controls		
Does legal counsel review all advertising and marketing materials with regard to the promises explicitly made or implied to customers?	<input type="checkbox"/>	<input type="checkbox"/>
Are you cautious of changing your accounts receivable collection procedures?	<input type="checkbox"/>	<input type="checkbox"/>
Do you seek legal counsel's assistance in developing sales and marketing training programs?	<input type="checkbox"/>	<input type="checkbox"/>
Do you require subcontractors and vendors supplying or doing work for you to name you as an additional insured on their E&O policies?	<input type="checkbox"/>	<input type="checkbox"/>
Do you obtain certificates of insurance from subcontractors and vendors?	<input type="checkbox"/>	<input type="checkbox"/>
Disputes & Allegations of Non-performance		
Do you carefully analyze all non-performance issues, claims and litigation as well as their causes?	<input type="checkbox"/>	<input type="checkbox"/>
If you have had product roll-backs or recalls in the past, have you documented why they occurred and the remedies used to resolve customer loss of use?	<input type="checkbox"/>	<input type="checkbox"/>
Do you examine and respond to the causes of any contract delays?	<input type="checkbox"/>	<input type="checkbox"/>
Do you have frequent and open discussions with your customers regarding the viability of any project as it progresses?	<input type="checkbox"/>	<input type="checkbox"/>

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