

Introduction

In order to assess the risks that our clients undertake when contracting with state and local governments, we reviewed the laws of the fifty states and the District of Columbia regarding the effectiveness of limitations of liability and exclusions of warranties. In most situations, limitations of liability will be enforceable. However, we have identified some instances in which courts may set aside mutually agreed upon limitations based upon public policy or an agreed upon remedy which the court finds to have failed.

The Uniform Commercial Code

All of the states, with the exception of Louisiana, have adopted some form of the Uniform Commercial Code ("U.C.C."). The U.C.C. is the governing law for the sales of goods. The U.C.C. generally favors the freedom to contract and supports the notion that commercial parties are allowed to allocate the risk of a contract as they decide. As such, most courts will enforce what the parties to a contract have agreed upon as long as that intent is clearly stated.

Section 2-719 of the U.C.C. allows parties to a contract to limit remedies available, as well as to limit consequential damages. Under the U.C.C., the standard for holding a limitation on consequential damages invalid is unconscionability. A contract clause is unconscionable if it is a one-sided, oppressive, and harsh agreement. This standard is primarily intended to protect innocent and unsophisticated consumers. Courts seldom find unconscionability in agreements between sophisticated commercial parties bargaining at arms' length.

Disclaimers or limitations of express and implied warranties are also generally enforceable under the U.C.C. if they are clear and conspicuous and consciously bargained for. The only state that differs markedly is Mississippi, which does not allow implied warranties ever to be disclaimed. However, Mississippi has made a statutory exception for computer hardware and software. The U.C.C. provides explicit guidance on what rules need to be followed in order for a warranty disclaimer or exclusion to be valid. The standard for enforcing a warranty disclaimer or exclusion is unconscionability.

The most significant disparity that we found concerned the issue of whether a consequential damages limitation is enforceable despite the fact that a limited or exclusive remedy has failed of its essential purpose. Section 2-719(2) of the U.C.C. states that a buyer is entitled to any U.C.C. remedy once a limited remedy has failed of its essential purpose. However, section 2-719(3) prevents a buyer from recovering consequential damages when they have been limited or excluded by the contract, unless it can be proven that the limitation or exclusion is unconscionable. Some state courts hold that the two sections are separate and independent provisions and that therefore, a consequential damages limitation will be enforced even if a remedy has failed of its essential purpose, unless that limitation is unconscionable as of the contract formation. Other states that have addressed this conflict hold that the two provisions are not separate and a buyer is able to recover consequential damages, despite a clause in the contract excluding them, if a limited remedy failed of its essential purpose. Some states, like Colorado and possibly Pennsylvania, would allow the consequential damages exclusion to remain valid so long as they can determine that the parties clearly and unambiguously intended that result.

Gross Negligence, Intentional Torts And Punitive Damages

Most courts look with disfavor on contract provisions that limit a party's liability for gross negligence, fraud, or intentional torts. Most of the states, however, have only addressed the issue of limiting gross negligence