Risk Allocation in Commercial Contracts

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Reviewed on: ***05/22/2019***

This practice note discusses common risk allocation mechanisms used in commercial contracts. It includes a discussion of how parties to an agreement can allocate risk by incorporating some or all of the following: a force majeure clause, an indemnification, a limitation on liability, termination rights, a Uniform Commercial Code (UCC) product warranty, detailed payment terms and guaranties, insurance obligations, and other contractual remedies. Practical guidance is included throughout this practice note.

For more related information, see *Avoiding Key Risk Allocation Pitfalls When Drafting Commercial Contracts*, and *Indemnification and other Contractual Provisions Checklist*.

Force Majeure Clauses

Force majeure clauses are an effective risk allocation tool and are permitted by both the UCC and the Restatement (Second) of Contracts. These provisions excuse a party's late performance or nonperformance for reasons outside its reasonable control. Force majeure clauses often require the affected party to (1) notify the other party in writing of the event of force majeure as soon as practically possible, and (2) use reasonable efforts to limit its impact on performance. Force majeure events can be natural or man-made, and generally include, by way of example: fire, earthquake, terrorist attacks, war, strikes, acts of God, and government orders. For related force majeure clauses, see *Force Majeure Clauses*.

Scope

The scope of a force majeure provision should be carefully considered by the parties' respective counsel in order to fairly allocate risk. Generally speaking, when an agreement requires all or most of its obligations to be fulfilled by one of the parties, that party's attorney should negotiate for a broad force majeure clause. The nonperforming party's counsel should, correlatively, push for (1) a narrow force majeure clause in order to limit the performing party's right to be excused from its obligations, and (2) the right to terminate the agreement if the event of force majeure continues for a designated period of time (see Termination for Cause under *Termination Rights*, below, for more information on this subject matter).

Necessity of Force Majeure Clauses

Many jurisdictions hold that a party's obligation to fulfill its contractual obligations is excused when performance becomes "impracticable." Pursuant to the *Section 2-615 of the UCC* and Section 261 of the Restatement (Second) of Contracts, impracticability occurs when a party's obligation to perform is made impracticable solely as a result of the occurrence of an event, the nonoccurrence of which was a basic assumption upon which the parties relied when entering into the agreement in the first place. In order to find impracticability, the following must be established: (1) the superceding event must render performance unduly burdensome (i.e., it can only be performed with unreasonable risk, expense, and/or difficulty); (2) the event's nonoccurrence must have been assumed by the parties when entering into the agreement (i.e., if the event was reasonably likely to transpire, it was *not* a basic assumption); (3) the affected party must not be responsible for the event's occurrence (including, without limitation, by failing to take reasonable measures to overcome the event); and (4) the added risk caused by the event must not have been allocated by the agreement to the affected party. As force majeure clauses typically reference only those events that fit the above description, the language may, arguably, be considered unnecessary. However, counsel should consider its inclusion for added protection.

Incomplete Listing of Force Majeure Events

It is virtually impossible to list every event rendering performance not practically possible when drafting a force majeure clause. Listing only certain events, however, can serve to exclude those which are not specifically referenced, rendering the affecting party responsible for non-enumerated occurrences. As such, the italicized language should be included in any well-drafted force majeure clause: "Neither party shall be held responsible for war, weather, strikes, lockouts, fires, acts of God, terrorism, *or any other activities or factors beyond its reasonable control, whether similar or dissimilar to any of the foregoing*."

Also, parties may wish to add certain, additional events to the list if and to the extent deemed important by their respective counsel given the nature and subject matter of the deal in question. For example, one or both parties may not be willing to assume particular market risks, such as foreign exchange rate fluctuations, computer failures, software glitches, or troubles with a supplier or distributor. The more specific counsel is as to the events covered, the better protection the language will provide his or her client. For more information on this topic, see *Force Majeure Clause Drafting*.

Indemnification Clauses

Indemnification clauses, also known as a hold harmless provisions, allocate the risk and expense arising out of a party's breach or misconduct. The primary benefit of an indemnification clause is to protect the indemnified party from losses incurred in connection with claims made pursuant to an agreement. Indemnifications can be mutual or one-way. In a mutual indemnification, each party agrees to compensate the other party for costs or damages arising out of the indemnifying party's breach, negligence, or misconduct. In a one-way indemnification, only one party provides this indemnity in favor of the other party. Indemnification clauses are typically heavily negotiated, and oftentimes heavily litigated, provisions. They are generally included in contracts where the risks associated with one or both of a party's breach or nonperformance are high. For example, contracts that involve the sale or license of intellectual property rights usually include an indemnification by the seller or lessor, as applicable, in order to protect the buyer or lessee, as applicable, against the potentially sizable liability associated with a third-party rights infringement lawsuit.

Counsel must ensure that the indemnity is tailored to his or her client's specific needs. For example, an indemnification can be restricted to particular third-party claims (i.e., breach of warranty), or limited to circumstances where a lawsuit has already been filed or a final judgment has already been rendered. Indemnifying parties generally control the defense of a claim since they are the ones paying for it. The notice requirement protects the indemnifying party from having to defend against a claim where it has been materially prejudiced by the indemnified party's delay in providing the indemnifying party with all requisite information about its existence and subject matter. Settlements most commonly require the approval of the indemnified party since its interests are directly at stake.

Scope of an Indemnification

The parties to an agreement must determine what types of liabilities will be covered by the indemnity. Generally speaking, indemnifications are drafted to cover material, uncured breaches, as well as negligence or willful misconduct. An indemnification clause can also exclude certain liabilities, such as taxes or pending litigation. They can also be limited to third-party claims (i.e., excluding direct claims between the parties). Each party's counsel should carefully weigh the risks and benefits associated with any such exclusions. Before agreeing to an indemnity, counsel must review it carefully and ensure that its client's obligations are limited to its own mistakes or misconduct. In the above example, the phrase "*to the extent arising out of*" helps to provide this limitation. In contrast, the phrases "*in any way arising out of*" or "*directly or indirectly related to*" could end up exposing a party to liability for the actions or inactions of the other party and/or a third party. The obligation to indemnify can also be limited by time (three or five years is most common). It can also be limited by dollar amount, although counsel should take great care in ensuring that the ceiling is sufficient to protect its client's interests. If the parties want the indemnifying party to cover the indemnified parties' legal fees as a reimbursable expense, counsel should ensure that this is stated in writing, as courts typically exclude their recoverability unless the agreement specifically provides otherwise. Counsel should also consider the possibility of having the indemnification serve as the sole remedy available to the indemnified party (see Exclusive Remedies Clauses under *Other Contractual Remedies* later in this practice note for more information on this subject matter). If, after considering the risks, the parties elect to include this concept, counsel should ensure that the language is clear and conspicuous, and that a cumulative remedies clause does not exist, as such a provision would directly contradict the stated limitation. Finally, counsel must consider what parties, in addition to the contracting parties, should be entitled to the indemnifications' protections (such as each other party's employees, agents, and directors, among others). This decision should be made after careful consideration of the particular risks involved in the transaction, including an analysis of which individuals and entities would most likely be affected by breach or misconduct.

The Enforceability of Indemnification Clauses

While indemnification provisions are typically enforced in court, there are exceptions to this general rule. For example, indemnities that require one party to indemnify the other party for *any* claim irrespective of fault (also known as "no fault" or "broad form" indemnifications) are typically held unenforceable for public policy reasons. Additionally, not all states permit indemnities that include punitive damages and as such, counsel must understand and ensure compliance with all applicable state laws as well as review the agreement's governing law. Furthermore, courts often deny recovery for damages that arise out of an improbable and unforeseeable result stemming from the other party's negligence, breach, or misconduct, other than in situations where the indemnifying party clearly had knowledge of the circumstances. Indemnifications must be drafted clearly, since ambiguity is most commonly resolved in the indemnifying party's favor. They should be sufficiently broad in order to address each party's basic needs, yet equitable enough so that their enforceability is not called into question. For more information on indemnities, see *Indemnity Provisions*, *Indemnification Provision Checklist*, and *Indemnification and other Contractual Provisions Checklist*. For related indemnification clauses, see *Indemnity Clauses*.

Limitations on Liability

A limitation of liability provision serves to limit a party's financial exposure in the event that a claim is made or a lawsuit is filed. It can be used to exclude one or both parties' liability for specific types of damages, such as indirect (including punitive damages, an otherwise standard tort remedy), consequential, and incidental, among others. It can also include a liability cap, often expressed as a multiple of fees paid pursuant to the agreement by one party to the other party. Counsel should ensure that the clause is appropriately tailored to meet its client's needs given the specifics of the deal in question. For example, a limitation of liability clause can apply to the agreement as a whole, or, alternatively, only to specific terms. Exceptions can be carved-out, such as making the limitation not applicable to either party's indemnification obligations. Additionally, limitations of liability can be mutual or one-way. They can also incorporate a statute of limitations.

Counsel should consider its client's role in the transaction in determining whether a limitation of liability makes sense or not, and if so, what terms would be most appropriate. For example, in a sale of goods agreement, the greatest risk is that the buyer will sue the seller for providing nonconforming merchandise, and as such, seller's counsel should push for the limitation on liability provision, while buyer's counsel should resist. Additionally, counsel should ensure that the language set forth in the limitation of liability is consistent with the terms of the agreement's indemnification clause and other contract provisions.

Insurance Requirements

Agreements often incorporate insurance obligations requiring one or both of the parties to obtain and maintain adequate insurance coverage. This serves to protect each party from the other party's inability to satisfy its financial liabilities under the applicable agreement (including its indemnification obligations). The types and minimum levels of insurance required depends upon the parties' needs, although general liability, employer's liability, and worker's compensation insurance are most commonly requested. Liability insurance policies cover amounts that an insured must pay to third parties for property damage or personal injury for which the insured is liable. For related clauses, see *Insurance Clauses* or *Insurance Covenant Clauses (Sale of Goods)*.

Parties to an agreement can, alternatively, agree to an insurance provision that simply affirms each other party's obligation to maintain "sufficient insurance coverage" to cover its obligations under the agreement.

Additionally Insured Status

The insured party will generally require the insurer to add it (and oftentimes its directors, employees, and affiliates) as an additionally insured party on all applicable policies. An additionally insured party is one who has direct rights in an insurance policy and as such, does not need to seek the consent of the named insured in order to get paid. The additionally insured party enjoys the same protections as the named insured party, including without limitation, defense, and indemnification. The additionally insured party, however, is also subject to the same policy limitations as the named insured and as such, counsel should ensure that his or her client maintains sufficient insurance coverage of its own.

Counsel should ensure that his or her client receive certificates to evidence that the proper coverage has been obtained by the other party pursuant to the agreement. The certificates should contain the following information:

- The full legal name of the insurance company
- The insured party's insured status
- The insurance policy number
- The policy period/term
- All applicable coverages
- All policy limits
- All defense obligation information
- All endorsement information –and–
- Any special considerations or other material terms

Quality of Insurance

The quality of the insurance company selected is crucial. If an insurance company goes bankrupt or is otherwise unable to meet its obligations as they become due, an insured party (as well as an additionally insured party) is not truly protected. For this reason, each party's counsel should require the other party to select an insurance company that meets certain objective performance measures or ratings as promulgated by one of several well-known companies. For example, A.M. Best Company, Standard & Poor's, and Moody's all provide insurance company ratings based upon financial size, claims-paying ability, and underwriting capacity, among other factors. These companies provide ratings for nationally based companies only. Additionally, the insured party's counsel should use best efforts to require the insuring party to obtain insurance with defense obligations that are outside (i.e., in addition to) the policy limits, as litigation costs are generally exorbitant and can easily exceed a settlement payment.

Nonrenewal, Material Change, or Cancellation

Each party's counsel should insist that the policies covering his or her client as an additionally insured party include a requirement to provide such client with not less than 30 days prior written notice of cancellation, nonrenewal, or material change. This is critical because if a policy is about to be cancelled as a result of the named insured's actions or inactions (including nonpayment of the premium), an additionally insured party may not necessarily be made aware of the situation on a timely basis. In such instances, the additionally insured would not be able to take the steps necessary to protect itself if the policy lapsed.

Policy Limits

Each party's counsel should ensure that the other party obtain adequate limits on the applicable insurance policies. Insurance limits dictate the maximum amount of money the insurance company will pay out in connection with a loss, including some or all of the following: (1) the number of total losses, (2) the number of claims that can be made, (3) the number of insureds covered by the policy, and (4) the number of persons or entities making claims. Additionally, insurance policies generally have multiple types of limits, such as per-occurrence limits and aggregate limits. A per-occurrence limit serves to cap the amount an insurance company is required to pay out for losses stemming from one event or a series of related events, depending on how the policy defines "occurrence." An aggregate limit serves to cap the amount an insurance company is required to pay out for losses for all occurrences combined. Each party's counsel should require the specific insurance limits to be stated in the contract, and the amounts should be sufficient to cover all reasonably known risks, taking into consideration the likelihood of damage or loss.

All insurance clauses should be reviewed by each party's internal risk management/insurance personnel for approval prior to contract execution. For more information on insurance clauses, see *Security Interest and Insurance Clauses — Drafting an Insurance Clause*.

Payment Terms and Guaranties

Detailed payment terms are often used by parties to an agreement to shift and control risk. Payments due under an agreement can be made either before or after the performing party has fulfilled its obligations.

Advance Payment Obligations

Advance payment obligations are either mandatory or optional. Mandatory advance payment clauses provide protection to the performing party against the risk of nonpayment, as delivery is made contingent upon receipt of the applicable purchase price. Such clauses are most commonly seen in sale of goods agreements where the merchandise is custom made. They are also commonly seen where the obligor needs the funds in advance of tender for one reason or another. Optional advance payment clauses permit (without requiring) a party to voluntarily pay some, or all, of the contractual amounts due prior to the performing party's fulfillment of its obligations, sometimes for a discount on the total invoiced amount. For more information on pre-payments, see *Voluntary and Mandatory Prepayments Clauses (Credit Agreement)*.

Deferred Payment Obligations and Guaranties

Deferred payment obligations are the norm in commercial transactions. For example, in a sale of goods transaction, buyers are generally not obligated to make payment until shortly after the seller has tendered the merchandise. Payment due dates are most commonly set forth in the applicable agreement, and typically require payment to be made within a certain number of days after the payor has received an invoice. The following is a sample deferred payment clause:

> "Payment: Client shall pay to Service Provider the monthly fee set forth above, subject to Client's receipt of an applicable invoice in connection therewith. Client shall have thirty (30) days following its receipt of each invoice to make such payment. A two percent (2%) discount shall apply in connection with pre-payments made by Client at least ten (10) days in advance of the applicable due date. Client shall be responsible for interest on all amounts overdue by at least thirty (30) days at a rate of the lesser of one and one-half percent (1.5%), or the maximum rate allowable by applicable law, along with all of Service Provider's reasonable and necessary collection costs, including without limitation outside attorneys' fees and expenses, incurred in connection therewith. If Client is delinquent in making payment for at least thirty (30) days, Service Provider shall also have

the right to: (i) suspend continued Services hereunder until such time as Client makes payment; or (ii) terminate this Agreement as provided for herein."

A seller of goods or services can minimize the risk of nonpayment by:

- Performing a credit check (along with other forms of due diligence) on the buyer/client
- Requiring payment to be made promptly after issuance of the invoice (obligors sometimes provide an incentive discount for payments made a certain number of days before they are due)
- Making a late or delinquent obligee responsible for interest payments and collection costs in connection with overdue amounts
- Providing for its right to suspend and/or terminate the agreement until payment is made (see Termination for Cause under *Termination Rights* later in this practice note) –and/or–
- Requesting a guaranty from the payor's parent company or investor/financier

Guaranties are most commonly required when a client's/buyer's creditworthiness or financial status is uncertain. They shift the risk of nonpayment from the obligor to the guarantor, benefitting both the obligor and the obligee. Guaranty clauses can either be incorporated in the applicable agreement between obligor and obligee, or set forth in a separate document to be executed by the guarantor and the obligee. If entered into pursuant to a separate agreement, the main contract should reference the guarantee, and the obligee should represent and warrant that it will obtain a written commitment from the guarantor that the guaranty will remain in full force and effect during the entire term of the underlying contract.

For more information on payments, see *Payment, Collection, and Audit*. For related payment clauses, see *Payment and Collection Clauses* and *Payment Terms Clauses*.

Termination Rights

Termination rights permit a party to terminate an agreement under certain circumstances, and fall into two main categories: (1) with cause, and (2) for convenience (i.e., without cause). Termination clauses can be unilateral or, more commonly, mutual. For related termination clauses, see *Termination Clauses*.

Termination for Cause

Termination for cause is where a party is entitled to terminate an agreement in response to certain events or actions, which generally include:

- A material uncured breach by the nonterminating party
- The negligence or misconduct of the nonterminating party
- A violation of applicable law by the nonterminating party
- The occurrence of an event that materially alters the nature of the agreement in general (such as an event of force majeure, which is discussed earlier in this practice note)
- The nonterminating party's severe financial distress –and–
- The high probability of material harm to the terminating party (i.e., such as reputational damage due to the nonterminating party's patently offensive behavior)

A clause granting a party the right to terminate an agreement based upon the other party's improper, offensive behavior is known as a "morals clause," and provides each party with an opportunity to proactively guard against actions taken by the other party that, while not necessarily illegal or in breach of the agreement between them, could hurt its image, brand, and reputation. Examples of behavior that invoke a morals clause include:

- Any arrest (regardless of whether a conviction ensues) for crimes of moral turpitude

- Documented incidents of driving while intoxicated
- Documented incidents of domestic violence
- Documented incidents of drug use or possession
- Public use of prejudiced language with respect to race/ethnicity, religion, gender, sexual orientation, and other similar bases
- Entering rehabilitation or seeking other treatment for drug or alcohol abuse
- Public recalls of a party's product or termination of a service for safety and similar legal issues
- Lawsuits and regulatory actions against a party –and–
- Association with controversial issues such as perceived government corruption, environmentally damaging practices, or use of child labor

The right to terminate for cause typically does not require advance notification (as the nonterminating party is most likely at fault for, and aware of, the circumstances triggering the terminating party's right in the first instance). When drafting a termination clause, each party's counsel should ensure that his or her client's particular concerns are addressed, given the specific risks involved in the transaction. For example, with an installment agreement, a seller should seek the right to terminate if the buyer fails to pay for one installment. Termination rights are not obligations, however, and as such, do not require the entitled party to terminate the agreement. Instead, the entitled party may:

- Request adequate assurances
- Suspend the agreement (if suspension rights are granted pursuant to the contract) until the situation is rectified
- Ignore the event giving rise to the entitled party's termination right –or–
- Avail itself or whatever other contractual remedies are available

For examples of demands for adequate assurances, see *Letter from Seller Demanding Adequate Assurances from Buyer* and *Letter from Buyer Demanding Adequate Assurances from Seller*.

Termination for Convenience

Termination for convenience (i.e., without cause, or "at will") provides a party with the right to terminate an agreement for any or no reason at all. Not all termination clauses provide for this right. A mutual provision allows either party to end a relationship that no longer serves it for one or more reasons. Most termination at will provisions require the terminating party to provide the other party with a certain number of days' advance written notice of its intention so that the nonterminating party has the opportunity to put into place alternative business plans and prepare to wind-down its current operations with the terminating party. Most termination for convenience clauses are upheld by courts, although they can be held unenforceable if determined to be unsupported by adequate consideration. Counsel for each party should ensure that its client is protected in the event of a termination at will by the other party by requiring the following:

- Advance written notification (90 days is the most common)
- Payment for all services rendered and expenses (including transition costs) properly incurred up through the effective date of termination
- Reasonable cooperation and assistance in transitioning work in progress to a third party, along with a prompt return of owned and/or paid for materials –and–
- Payment of an appropriate termination fee

For related termination provisions, see *Termination Clauses*.

UCC Product Warranties in Sale of Goods Agreements

Product warranties are governed by *UCC Sections 2-312 through 2-318* (for sale of goods) and *UCC Sections 2A-210 through 2A-215* (for equipment leases). They can be used to effectively allocate certain risks between buyers and sellers. There are two main types of product warranties: (1) express and (2) implied. They are provided at law, and as such, unlike transactional representations & warranties, do not need to be included in the applicable contract. For more information on contractual representations & warranties, see *Commercial Agreement Representations, Warranties, Covenants, Rights, and Conditions*. See also the section entitled Representations and Warranties under *Other Contractual Remedies* later in this practice note.

Express Warranties

An express warranty is a promise or guarantee by the seller that the merchandise being sold is or will be provided to the buyer as promised (i.e., that the product in question will meet a certain threshold of quality and reliability). The words "guarantee" or "warranty" do not have to be included in an express warranty. A buyer may rely upon any express warranty provided by a seller when purchasing goods from the seller. Express warranties can be found:

- In the sales agreement
- In the merchandise's product warranty
- By way of an affirmation of fact ("The raincoat is 100% waterproof") (*UCC § 2-313(1)(a)*)
- By way of written or verbal description ("The game, when played correctly, shouldn't take more than one hour to finish") (*UCC § 2-313(1)(b)*)
- By way of an oral promise ("This coat will not shrink") (*UCC § 2-313(1)(b)*) –or–
- By way of having provided the buyer with a mock version or tester (*UCC § 2-313(1)(c)*)

Express warranties can easily be made unintentionally and as such, each party's counsel should (1) include all express warranties in writing in the applicable agreement, and (2) disclaim the existence of any other express warranties, however potentially made, other than those provided in writing in the agreement. Express warranties should never cover problems that occur outside of a seller's control, including normal wear and tear, misuse, and/or the performance of unauthorized repairs, to name a few. Seller's counsel should look to limit the warranties that it provides, while buyer's counsel should ensure that the warranties provided are sufficient to cover his or her client's needs. A seller can restrict the scope of the express warranties provided by including (1) a time limitation on each such warranty; (2) conditions that may invalidate any such warranty (such as mishandling, misuse, and faulty repair); and (3) exclusive remedies for breach (see Exclusive Remedies Clauses later in this practice note for more information on this subject matter). For more information on UCC Article 2 express warranties, see *Uniform Commercial Code Article 2 Express Warranties*. For more information on UCC Article 2A express warranties, see *UCC Article 2A Express and Implied Warranties*.

Implied Warranties

Implied warranties are those imposed by operation of law, custom, or the conduct of the parties, regardless of whether they are also expressly provided (i.e., either verbally or in writing). They are imposed unless expressly and properly disclaimed (i.e., in a clear and conspicuous manner) in the applicable agreement. Text that stands out against the remainder of the document generally suffices (i.e., ALLCAPS, **bold**, or *italics*). Additionally, counsel must understand and comply with all specific UCC language requirements in order to create enforceable disclaimers.

The implied warranties imposed by operation of law include (1) the warranty of merchantability (*UCC § 2-314*), which is based upon a buyer's reasonable expectation that the goods are fit for the ordinary purpose for which they were meant to be used and not defective; (2) the warranty of fitness for a particular purpose (*UCC § 2-315*), which is based upon the seller's provision of goods that are suitable for the buyer's known, specialized needs; (3) the warranty against infringement (*UCC § 2-312*), which is based upon the seller's obligation to provide goods that are free of any rightful claims of third-party infringement; and (4) the warranty of title (*UCC § 2-312*), which is based upon the seller's obligation to provide goods that are free from any security interest or other lien or encumbrance. With respect to equipment lease agreements as governed by UCC Article 2A, the warranty of title is replaced with a warranty of quiet possession.

Other implied warranties include those imposed by (1) course of performance (*UCC § 1-303(a)*), which is based upon a sequence of conduct between the parties to a transaction that exists if the agreement involves repeat performance one party to the other, and with knowledge of the nature of the performance and an opportunity to object to it, the other party accepts it (or acquiesces without objection); (2) course of dealing (*UCC § 1-303(b)*), which is based upon the parties having certain reasonable expectations based upon their previous pattern of dealings with one another; and (3) course of usage of trade (*UCC § 1-303(c)*), which is based upon a pattern of conduct that conforms to standard practice in a particular vocation, trade, or place, thereby justifying the parties' expectation that the pattern will continue with respect to the transaction in question.

Limited Warranties

Sellers commonly provide a limited warranty in connection with the merchandise that they sell. The following is an example of a limited warranty which incorporates disclaimers and exclusive remedy language (for more on exclusive remedies, see Exclusive Remedies Clauses under *Other Contractual Remedies*, below):

> "Limited Warranty:
>
> (a) COMPANY'S LIMITED WARRANTY: We represent and warrant to you that any goods purchased by you on the Site, when used specifically as authorized by us and without modification thereto, will conform in all material respects to: (i) the specifications set forth on the Site, and (ii) any instructions that we provide you with upon delivery of the merchandise. We further represent and warrant to you that any goods or services purchased by you on the Site will be safe for their intended use and free from defects in material, functionality, and workmanship. Notwithstanding the foregoing, this warranty shall not apply when the goods are subject to: negligence, misconduct, misuse, abuse, accident, improper installation or handling, unusual environmental conditions, or other extreme stress, alteration, repair by anyone other than us (or one of our authorized representatives), use with any third-party product or service (other than as specifically authorized in advance by us), or use in violation of any provided-for instructions [(including without limitation any license agreement)]. Notwithstanding the foregoing, any products manufactured by a third party and incorporated in any goods provided hereunder are not covered by this limited warranty. We further warrant to you that we will perform any services purchased through the Site using personnel of all required skill, experience and qualifications and in a professional manner in accordance with generally recognized industry standards for similar services in order to meet our obligations hereunder. Notwithstanding anything set forth herein to the contrary, your sole remedy with respect to a breach by us of our warranties to you shall be to inform us, in writing, of your desire to exercise this limited warranty, along with a sufficiently detailed explanation of your reason(s), so that we may either: (i) repair or replace the goods in question (or re-perform the services, as applicable); or (ii) credit or refund your purchase price. In such instance, restocking fees shall not apply. We shall have the right to select which cure option to pursue, and we will be responsible for shipping & handling charges associated with resending replacement goods (and shall also be responsible for their risk of loss in transit during such time), if and as applicable. Any claim made by you hereunder shall be made within _______ (_) [days/weeks/months] following the time when you actually discovered, or should have discovered, any defect(s) or non-conformance. We reserve the right to verify any such claim pursuant to our customary procedures in connection therewith. This warranty period is not extended if we have to repair or replace a warranted product or re-perform a warranted service. This limited warranty extends only to you as the original purchaser of our products and services from our Site (i.e., and not to any subsequent owner or beneficiary of any goods or services received hereunder). In order to obtain warranty service, please contact [INSERT CONTACT INFORMATION HERE] and obtain an RMA number. For further details on how to exercise your rights hereunder, please review the information set forth at the following: [INSERT URL ADDRESS]. If for any reason you believe in good faith that we have not fulfilled our obligations hereunder, you are entitled to follow the dispute resolution procedures set

forth in below. THIS LIMITED WARRANTY CAN ALSO BE FOUND AT [INSERT URL ADDRESS] AS WELL AS IN THE DOCUMENTATION WE PROVIDE WITH THE PRODUCTS.

(b) LIMITATION ON WARRANTIES: Subject to applicable law and the terms hereof, we make no express or implied warranty whatsoever with respect to the goods or services purchased through the Site, including without limitation any: (i) warranty of merchantability; (ii) warranty of fitness for a particular purpose; (iii) warranty of title; or (iv) warranty against infringement of intellectual property rights of a third party, whether express or implied by law, course of dealing, course of performance, usage or trade, or otherwise.

(c) SOLE AND EXCLUSIVE REMEDIES/LIABILITY CAP: SUBJECT TO APPLICABLE LAW, THE REMEDIES SET FORTH ABOVE ARE YOUR SOLE AND EXCLUSIVE REMEDIES, AND OUR ENTIRE OBLIGATION AND LIABILITY, FOR ANY BREACH OF OUR LIMITED WARRANTY. SUBJECT TO APPLICABLE LAW, UNDER NO CIRCUMSTANCES WILL COMPANY'S OBLIGATION OR LIABILITY HEREUNDER EXCEED THE PURCHASE PRICE YOU PAID ON THE SITE FOR ANY GOODS OR SERVICES. ADDITIONALLY, SUBJECT TO APPLICABLE LAW, UNDER NO CIRCUMSTANCES WILL WE BE LIABLE FOR ANY LOSS OF USE, DATA, BUSINESS, GOODWILL, REPUTATION, OR REVENUE, AND/OR ANY CONSEQUENTIAL, INCIDENTAL, SPECIAL, OR PUNITIVE DAMAGES OR OTHER DIRECT OR INDIRECT LOSSES OF ANY KIND."

Counsel must ensure that all warranties of any kind or nature comply not only with the UCC but also with all applicable federal and state laws (including without limitation the Magnuson-Moss Warranty Act (*15 U.S.C. § 2301 et seq.*)). For more information on the Magnuson-Moss Warranty Act, see *Magnuson-Moss Warranty Act* and *Consumer Product Warranties under the Magnuson-Moss Warranty Act Checklist*. For a product warranty, see *Full Consumer Product Warranty* and *Limited Product Warranty*. For more information on both express and implied warranties, see *Responding to Claims That Goods Do Not Conform to Warranties Checklist*.

Other Contractual Remedies

There are a host of other contractual remedies that serve to allocate risk in commercial contracts.

Equitable Remedies

Equitable remedies are nonmonetary remedies that require a party to take a specific action or set of actions in order to make the other party whole. They are not automatically available but rather, enforced and/or awarded in a court's discretion where it has been determined that monetary damages are either unavailable or insufficient. Examples of equitable remedies include, without limitation: (1) injunctions, (2) reformations, (3) specific performance, and (4) rescissions and restitution. Contracts can either permit or prohibit equitable remedies, yet the court system will ultimately determine the appropriateness and enforceability of their applicability.

Each party's counsel should carefully weigh the pros and cons of permitting or prohibiting the different forms of equitable relief given the specific facts of the transaction in question. For related equitable remedies clauses, see *Equitable Remedies Clauses*. For related "no equitable remedy" clauses, see *No Equitable Relief Clauses*.

Cumulative Remedies Clauses

A cumulative remedies clause provides that all of the rights and remedies set forth in the applicable contract are cumulative (i.e., that they can be obtained in addition to whatever implied rights or remedies may be provided at law or in equity). An obligee generally favors a cumulative remedies clause, as it provides for the widest range of remedies in the event of a breach by an obligor. An obligor typically prefers an exclusive remedies clause in order to minimize its assumed risk exposure and potential liability (see Exclusive Remedies Clauses under *Other Contractual Remedies*, below, for more information on this topic). Counsel should ensure that if incorporating a cumulative remedies clause, the language does not contradict any other contractual provision, including without limitation the indemnity (see *Indemnification Clauses*, above) and liquidated damages clause (see Liquidated Damages under *Other Contractual Remedies*, below). Additionally, exceptions can be carved-out from cumulative remedies clauses. For related cumulative remedies clauses, see *Cumulative Remedies Clauses*. For more information on this topic, see *Remedies*.

Exclusive Remedies Clauses

An exclusive remedies clause is the opposite of a cumulative remedies clause—it limits an obligee's available remedies in the event of a breach by obligor. Without such a clause, a court may find that the remedies provided for in the applicable agreement are in addition to any and all implied rights or remedies that may be provided at law or in equity (i.e., instead of in lieu of such implied rights or remedies). Examples of clauses that often include an exclusive remedy provision are indemnifications (see *Indemnification Clauses*, above) and liquidated damages clauses (see Liquidated Damages under *Other Contractual Remedies*, below). Obligors typically favor exclusive remedies provisions as they limit risk exposure, while obligees generally favor cumulative remedies clauses as they provide for the greatest breadth of recovery in the event of an obligor's breach. Agreements can include both a cumulative remedies and an exclusive remedies provision, although counsel must ensure that they do not contradict each other (i.e., the language must clearly delineate which remedies are cumulative and which are exclusive). Ambiguous drafting may be resolved by a court in a manner that the parties did not intend at the time of contracting. For more information on this topic, see *Remedies*.

Liquidated Damage Clauses

Liquidated damage clauses are often used to define recoverable damages when they would otherwise be difficult or impossible to calculate (for example, a lost business opportunity). They minimize the risk of a dispute over the amount of damages that would be appropriate in the event of a breach or default by a party. The uncertainty is eliminated. If the parties to an agreement desire the inclusion of a liquidated damages clause, counsel should make it clear that the damages are: (1) an exclusive remedy (see Exclusive Remedies Clauses under *Other Contractual Remedies*, above); and (2) compensatory and not punitive, as courts will not enforce punitive damage clauses. For more information on liquidated damages, see *UCC Liquidated Damages*.

Representations and Warranties

Representations and warranties are standard contractual provisions that serve to provide the non-representing party with assurance of specific facts and conditions from the representing party, the failure of which provides a valid breach of contract claim in favor of the non-representing party. For related clauses, see *Representations and Warranties Clauses*.

Each party's counsel should ensure that the other party provides adequate representations and warranties given the nature and specifics of the deal in question in order to maintain sufficient breach of contract remedies. For more information on contractual representations & warranties, see *Commercial Agreement Representations, Warranties, Covenants, Rights, and Conditions*.

Related Content

Practice Notes

- *Risk Assessment*
- *Force Majeure Clause Drafting*
- *Merger Clause and Force Majeure Clause Drafting*
- *Indemnity Provisions*
- *Indemnification Provisions in Commercial Contracts*

- *Payment, Collection, and Audit*
- *Commercial Agreement Representations, Warranties, Covenants, Rights, and Conditions*
- *Uniform Commercial Code Article 2 Express Warranties*
- *UCC Article 2A Express and Implied Warranties*
- *Magnuson-Moss Warranty Act*
- *Remedies*
- *UCC Liquidated Damages*
- *Outsourcing: Scope, Service Levels, Risk Allocation, and Price*

Annotated Forms

- *Force Majeure Clauses*
- *Indemnity Clauses*
- *Insurance Clauses*
- *Insurance Covenant Clauses (Sale of Goods)*
- *Security Interest and Insurance Clauses*
- *Voluntary and Mandatory Prepayments Clauses (Credit Agreement)*
- *Payment and Collection Clauses*
- *Payment Terms Clauses*
- *Termination Clauses*
- *Letter from Seller Demanding Adequate Assurances from Buyer*
- *Letter from Buyer Demanding Adequate Assurances from Seller*
- *Full Consumer Product Warranty*
- *Limited Product Warranty*
- *Equitable Remedies Clauses*
- *No Equitable Relief Clauses*
- *Cumulative Remedies Clauses*
- *Representations and Warranties Clauses*
- *Limitation of Liability Clauses (Distributors)*

Checklists

- *Avoiding Key Risk Allocation Pitfalls When Drafting Commercial Contracts*
- *Risk Assessment Information and Document Review Checklist*
- *Risk Assessment Sample Questions Checklist*
- *Risk Assessment Topics to Review Checklist*
- *Indemnification Provision Checklist*
- *Indemnification and other Contractual Provisions Checklist*
- *Commercial Contract Drafting and Review Checklist*
- *Consumer Product Warranties under the Magnuson-Moss Warranty Act Checklist*
- *Responding to Claims That Goods Do Not Conform to Warranties Checklist*

Resource Kits

- *General Commercial Contract Clause Resource Kit*
