

# Piggy in the middle?

Alice Rayman of **The Simkins Partnership** takes a practical look at agency liability under client contracts

**T**he section of any contract which induces the greatest level of confusion and lack of interest is the section headed 'Limitation of Liability' – or sometimes 'Liability and Indemnity', since those words are occasionally used interchangeably. In addition, the term '*Force majeure*' is treated as at once a mystery and a 'boilerplate' clause. Yet these clauses cover key issues in any relationship between two parties in business, and should be focused on carefully.

The relationship between an advertising agency and its client is a good example to examine, because of the way in which their arrangements are generally structured. Despite the name 'agency', an advertising agency usually carries out work for its clients by entering into contracts with third parties as 'principal', ie in its own name rather than the client's. Talent contracts with celebrity artists with whom the client wants a personal relationship might be the exception.

It is critical for an agency to understand the nature and extent of its liability to its client, and where it might incur liability in its dealings with third parties on behalf of its client. This article does not propose to look at the detail of different types of loss, but rather to provide a practical warning as to how agencies can be exposed – and offer a few tips on how to minimise the risks.

## The industry standard agency/client contract

The advertising business operates to well-established practices to the extent that its industry body, the IPA, has negotiated with the advertiser's representative body (ISBA) a standard contract for agencies to use with clients. The contract is widely used – as a starting point for a first draft, even if not in its entirety – so it is useful to look at how it deals with liability.

The contract (see box, below) provides for the agency's liability to be limited in terms of the type of loss which might be suffered by the client (para 2) and the amount of loss (para 1). However, rather than looking in detail at all the implications of this wording, I will move on to how the contract is generally handled, and then to the agency's other contractual relationships.

## The client contract

The client contract is, unsurprisingly, regarded as the agency's most important

contract: the commercial negotiations over fees and scope of work are dealt with at the account-handling level, perhaps with help from the finance director on the detail of the contract. The principal aim is to get the fee agreed and keep the client happy. Where possible, the kind of limitations of liability set out in the IPA contract are used or at least tried for, but in delicate negotiations with clients the agency's fee and scope of work is generally likely to take higher priority than an esoteric legal discussion of risk in a meltdown situation – which nobody wants to think about anyway.

## The work and third-party supply contracts

Aside from the talent contracts referred to above, what other business does the agency conduct in providing advertising services to its client? Its role is to come up with creative ideas, plan a campaign in various media and execute those ideas by producing the ad and getting it on air or into the media. The first

## AGENCY LIABILITY UNDER THE IPA/ISBA STANDARD AGENCY CONTRACT

### Limitation of Liability

Nothing in this Agreement shall exclude or in any way limit the Agency's liability for fraud, or for death or personal injury caused by its negligence, or any other liability to the extent such liability may not be excluded or limited as a matter of law. Subject to this but including any liability arising under any indemnity under this Agreement:

1. the Agency's maximum aggregate liability under or in connection with this Agreement, whether in contract, tort (including negligence) or otherwise, will in no circumstances exceed [the total charges payable to the Agency hereunder during the preceding 12 months] [£...]; and
2. the Agency will not be liable under this Agreement for any loss of actual or anticipated income or profits, loss of contracts or for any special, indirect or consequential loss or damage of any kind howsoever arising and whether caused by tort (including negligence), breach of contract or otherwise, whether or not such loss or damage is foreseeable, foreseen or known.

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two elements are generally performed in-house by the agency's staff. The rest is very often a matter of contracting third party suppliers. These include the production company, printers, media owners, research organisations and software developers for the design of websites.

For example I recently reviewed a web design contract for an agency, where it was commissioning software design for a client website. The clause relating to liability provided:

Except in respect of death or personal injury caused by Supplier's negligence, the entire liability of Supplier for any and all claims by the Agency under or in connection with this Agreement whether in contract, by reason of negligence or otherwise, or whether related to any single event or a series of connected events shall not exceed the Service Charges.

Supplier excludes any liability for any loss of revenue, loss of data, loss of profits, loss of business or goodwill, business interruption or for any types of anticipated or incidental losses such as loss of anticipated savings or loss of third-party contract profits even if Supplier had notice (implied or actual) of the possibility of the Agency incurring such losses. Supplier excludes all liability for any type of indirect or consequential loss however caused.

Supplier shall have no liability to the Agency for any loss or damage arising from the Company Materials or instructions supplied by the Agency

which are incomplete, incorrect or inaccurate, illegible or arising from their late arrival or non-arrival, or any other fault of the Agency.

Now we have to think about whose liability is at issue here – the supplier's. What is the import for the agency if the supplier's liability is limited to a different degree to its own liability to the client? Obviously, the agency could incur liability (to the client) which it cannot recover from the supplier. Hopefully the insurance will cover it – more on that later.

You can see at a glance that while most of the same types of loss may be covered here

even be a limitation of liability clause in the client contract, in which case the law governing recovery of damages for breach of contract would apply to the client's claim.

As a matter of practice, contracts with suppliers are negotiated (at least in respect of the commercial terms) by individuals in the agency who work in the area buying those supplies – not the account team, in any event. Also, as a matter of practice, the contract used is often the standard contract of the supplier, which for speed and ease agency personnel agree to use (subject to negotiation, to a greater or lesser extent).

The degree to which the contract will be reviewed by the agency's finance director or

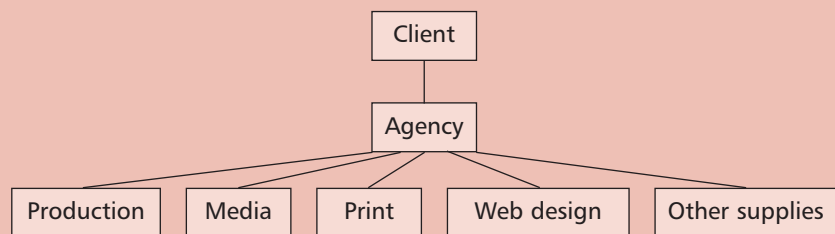
**'It is critical for an agency to understand the nature and extent of its liability to its client.'**

as in the IPA client contract, the clauses are drafted by a different hand, so it will take some careful checking to ensure that they are in fact covered. Certainly, any monetary cap will be different if based on the contract price – fee payable by client to agency as against fee payable by agency to software developer. So, from this example it is clear that if the client had a large claim against the agency in connection with the website – eg it crashes and sales made over the Internet are lost, a third-party trade mark is wrongfully used on the website, etc – the agency might have to pay out to the client and only be able to recover a fraction of that amount from the supplier. There might not

any other person with a good knowledge of contract law and risk management will depend upon the size of the agency and the perceived importance of the contract in question. Not surprisingly, most people measure the importance and value of a contract by the amount of money being paid for the goods or services to which it relates. A contract for which a few thousand pounds are paid for website maintenance will not in many cases be deemed worthy of scrutiny by the legal department or external lawyers.

Another way of looking at a contract, however, is to consider the risk to the agency if the supplier failed to perform. Of course, there are agencies where every contract is scrutinised by the person with responsibility for legal matters. However, even if that is the case, does that person go through the thought process of possible risk to the agency in a disaster scenario, across the network of contracts that makes up the agency's work for any one client, and consciously consider that against the provisions of the relevant client contract (which may or may not have been signed by the time work with suppliers starts)? It

## AGENCY CONTRACTUAL RELATIONSHIPS



would be unusual if the answer to that question were 'yes'.

### **Force majeure**

I only mentioned this because too often it slips through the net. If those negotiating the contract understand clearly what is meant by *force majeure* as a principle, they are likely to believe that it is reasonable for the principle to apply and at the same time to assume that the clause in the contract they have in front of them is standard wording which does not need close examination. This could not be further from the truth.

A *force majeure* clause is an example not only of a limitation, but an exclusion of liability for the supplier in certain circumstances. Where the cause of the supplier's failure to perform is accepted to be 'beyond its control', the supplier will not be liable for damages for breach of contract. In the circumstances being considered here, the agency needs to consider whether it is reasonable for the supplier not to be liable for damages at all. The answer may be yes – but if so, is it clear in what circumstances the supplier would be let off the hook?

This comes down to the definition of '*force majeure*', which varies from contract to contract but in any case often sweeps up with 'and any other events generally treated as *force majeure*' or similar wording. Is the failure of a third party to perform a contract to which the supplier is a party a reasonable *force majeure* event? It is often listed as such. What does it mean? If the supplier's electricity fails and it cannot operate its computers, is it reasonable? What would be the impact on the agency? Does its client contract let it off the hook in those circumstances? What if the supplier's contracted delivery company does not turn up on time and as a result the agency cannot meet a deadline? Should it be the supplier's responsibility to ensure its own suppliers perform – should the agency suffer in those circumstances? What happens if the *force majeure* event continues for a long time? The agency would not necessarily be entitled to terminate the contract – the clause should state that after a given period the agency is entitled to terminate.

### **Insurance**

In many of the situations highlighted here, insurance will save the day. But it is critical that those dealing with the contracts give some thought to whether or not that is the case. It is possible that the risk itself might not be covered. For example, sometimes there is a gap between the production company's cover for an artist on set and the extent of the agency's cover for getting the artist to the set. Who is covering the artist if they are injured while on a day's shoot but not actually on set?

But there is another consideration: even agreeing to a limitation of liability in a contract with a supplier – or not insisting on one in the client contract – can create problems under the terms of an agency's

silent on limitation of liability but has an indemnity clause with a limit in it, this does not mean that the agency's liability is limited overall. It just means that the amount the client can recover from the agency on an indemnity basis is limited: the client might still be able to sue the agency for any excess of its loss above the cap on the basis of a claim for damages for breach of contract. This is a common cause of misunderstanding among non-lawyers negotiating contracts.

### **Minimising the pitfalls**

The point I wish to highlight is that the operation of the agency's business is a nexus of contractual arrangements, all potentially giving rise to liability on the part of the

## 'Is the failure of a third party to perform a contract to which the supplier is a party a reasonable *force majeure* event?'

insurance policy. I have seen a group policy which required a paper trail of evidence that the agency had tried to negotiate no (or as little as possible) limitation of liability in its contracts with suppliers. Provided that was there, it was acceptable for the liability to be limited. The person negotiating the contract was not aware of this requirement. Other policies might impose harsher requirements.

### **Indemnity**

Just one word on this: there is sometimes confusion about the meaning of indemnity. As most readers will be aware (among other distinctions) it determines the amount of the client's loss that can be recovered under the contract, as distinct from the loss which may be recovered by means of a claim for damages for breach of contract. It is possible to cap the amount or type of loss that can be recovered in this way. But such a limit should not be confused with a limitation of liability. If the contract is

agency to its client, because the agency stands between the client and its suppliers. These contractual arrangements are made by different people with different focuses, priorities and levels of awareness.

Ideally, one person should be aware of all the issues surrounding each such contract and consider the issue of liability under all of them – and that person should be familiar with the agency's client contract and insurance policy. If that is impractical, some headline advice should be given to agency personnel negotiating contracts day to day to alert them to the issue of liability, any cap that is or is not acceptable, and any basic requirements of the insurance policy. The risk in any one case may be minimal but someone needs to consider it before the contract is signed and the work is begun.

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