

Liquid(ated) damages

When numerous safety measures fail to prevent damage to property, just how much of the losses can be recovered? **Alan Ma** examines a blurry aspect of contract law



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Even if losses are caused by a breach of contract, they cannot be recovered if they are too remote. But the exact boundary of recoverable losses has always been controversial.

Earlier this year, the Court of Appeal gave judgment in the case of *Supershield v Siemens Building Technologies FE* on whether losses are recoverable when the losses caused by the initial failing should have been averted by other fail-safe measures – which also failed.

Supershield was a subcontractor of Siemens in the construction of an office building. It had to install a ball float and lever arm so that the water storage tank of a sprinkler system would be refilled whenever the water level dropped, just as applies in a domestic toilet cistern. *Supershield* failed to install the ball float and lever arm properly. The nut and bolt did not connect with each other and the bolt fell out. As a result, the valve was left open so that water flowed into the tank and the valve did not close as the tank filled up. The tank overflowed.

The design of the building had fail-safe measures in place, including drains in the tank room and alarm systems in the building. But the drains became blocked and the alarm system was not being monitored. Water flooded from the tank room into the basement and caused substantial damage to electrical equipment.

Was the damage caused by the escape of water from the tank too remote? The foundation of the law can be traced back to a case from 1854. The test laid down by

the court is that the loss is not too remote if either (a) it naturally followed the contract breach; or (b) it was within the reasonable contemplation of both parties at the time they made the contract.

The novelty of *Supershield* is that there was a simultaneous failure of separate protection measures. The court considered the purpose of the contract and the scope of the contractual obligation form the basis of deciding remoteness. The ball valve was the first means of protection against water causing damage to other parts of the building and it failed. It follows the loss was within the scope of the contractual obligation and it cannot

be regarded as too remote, even if it would not have occurred in ordinary circumstances.

The lesson learnt from *Supershield* is that the objectives and the scope of work should be clearly stated within the contract to avoid uncertainty as to whether losses are recoverable should the contract fail.

Given losses are not too remote if they are within the reasonable contemplation of the parties when the contract was entered into, parties are free to stipulate the types of loss that may result should the contract fail. Examples of losses

include damage to property, loss of profits and incurring extra financial charges.

It is open to parties to pre-estimate the loss which they believe that a breach of contract will cause, and may contract for a particular measure of damage to be payable on that breach. A schedule specifying these details may be attached to the contract. Such a clause is described as a liquidated damages clause and the court will hold parties to their bargains.

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