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Even Limitation of Liability Clauses Have Limitations

By Toby Butterfield, Rebecca Diamond, and Allan Grauberd | June 26, 2026

When sophisticated parties prepare a commercial contract, countless hours are poured into the "sub stantive" terms. But when it comes to "boilerplate" provisions like limitation of liability clauses, drafters often lose steam. "Form" language is inserted without adequate consideration—the parties, eager to begin their relationship, hope they will never need to worry about these provisions.

This approach can have significant negative conse quences. The law concerning limitation of liability clauses is strict, and business leaders and their counsel must resist the urge to assume that such clauses carry their preferred meaning.

What is a Limitation of Liability Clause?

A limitation of liability clause caps the amount and types of damages one party may be required to pay the other in the event of a breach. These provisions provide the parties with a clearer understanding of "worst-case scenario" consequences. They often exclude categories of damages such as lost profits and consequential damages, and may inadvertently limit the contract price to be paid.

What Should Limitation of Liability Clauses Actually Do?

Limitation of liability clauses are essential risk management tools. If drafted correctly, they cap financial exposure, exclude certain damages, allocate risk appropriately, and provide predictability. But common pitfalls can erode their efficacy and lead to detrimental outcomes.

Examples are:

· Unclear Language: Using vague, unclear or imprecise language that is not properly tied to the rest of the contract, including the defined terms, can result in inconsistent outcomes that render the provision entirely unenforceable.

· Reliance on Templates: There is a tendency to rely on templates without customization. These forms will undoubtedly fail to account for the nuances of a particular deal, and should not be inserted without adequate modification.

· Failure to Consider Potential Risks: Many drafters either fail to consider all potential risks, inadvertently exclude relevant liabilities, or alternatively lump all damages into one general exclusion, which courts sometimes deem too unclear to be enforceable and/or be limited by a court, to avoid it being overbroad.

· Relation to Contract Price: From the perspective of the party expecting to be paid, a limitation of liability provision should never relate to the contract price itself, as this can undermine the agreement's main purpose. Non-payment of the purchase price is itself a breach giving rise to liability. Language should make clear that the limitations clause does not limit liability for payment of the contract price. Otherwise, seemingly standard limitations—such as capping total liability at amounts paid over the life of the contract—can become an effective "option to terminate" by a party who decides to exit a long-term contract after only a few payments.

· One Size Does Not Fit All: Parties often adopt a "one size fits all" approach to risk allocation. Limitations should reflect a fair balance of risk depending on relative bargaining power and the nature of the deal.

A bilateral approach is almost never the answer.

In almost every contract there is a financial obligation owed to a service or product provider; that liability should not be affected by a limitation of liability clause unless the service or product is deficient. Protections for deficiency should be handled outside the limitation of liability clause, such as in warranty provisions.

When they are implicated in the limitation of liability clause, confusion and unintended consequences often ensue. Properly drafted clauses should exclude matters related to the agreed contract price.

The Consequences of Overbroad Drafting

Drafting a limitation of liability clause without careful attention to its scope can lead to significant consequences. A poorly drafted clause may be rendered unenforceable, lead to unintended liability exposure, or improperly cap liability when significant harm occurs. New York jurisprudence provides both guidance and cautionary tales.

Under New York law, for a contractual limitation of liability to be enforceable, it must be unambiguous, explicit and clear. Terminal Cent., Inc. v. Henry Modell & Co., Inc., 212 A.D.2d 213, 218-19 (1st Dep't 1995); PRO Net, LLC v. ACC TeleCom Corp., 294 A.D.2d 857 (4th Dep't 2002); 1861 Cap. Master Fund, LP v. Wachovia Cap. Markets, LLC, 95 A.D.3d 620, 621 (2012). These clauses are strictly construed against the party seeking to avoid liability. Terminal Cent., Inc., 212 A.D.2d at 219. Other states' laws contain similar requirements, though precise interpretation standards vary state-to-state.

New York courts regularly strictly enforce limitation of liability provisions drafted by sophisticated parties, viewing them as the parties' agreement on risk allocation. Process Am., Inc. v. Cynergy Holdings, LLC, 839 F.3d 125, 138 (2d Cir. 2016); Metro. Life Ins. Co. v. Noble Lowndes Int'l, Inc., 84 N.Y.2d 430, 436 (1994). This underscores the importance of carefully considering these provisions, as courts will look to the contract terms with little sympathy for poor drafting.

In Metropolitan Life Insurance v. Noble Lowndes International, Inc., the Court of Appeals held that sophisticated parties may agree to limit recoverable damages. Metropolitan Life Insurance v. Noble Lowndes International, Inc., 84 N.Y.2d 430 (1994). The software license agreement at issue contained a provision releasing the licensor (defendant) from damages for lost profits, loss of business, or other financial loss resulting from performance or nonperformance, except for intentional misrepresentations or damages arising from willful acts or gross negligence.

The licensee sued seeking consequential damages from the licensor's withdrawal from the contract. The Court of Appeals reduced damages to the amount paid to the licensor, holding that the "willful acts" exception did not apply because the licensee failed to establish willful intent to inflict harm.

The court stated: "[a] limitation on liability provision in a contract represents the parties' agreement on the allocation of the risk of economic loss in the event that the contemplated transaction is not fully executed, which the courts should honor.... [The parties] may later regret their assumption of the risks of non-performance in this manner; but the courts let them lie on the bed they made."

Similarly, in Process America Inc. v. Cynergy Holdings LLC, the Second Circuit enforced a limitation of liability despite argument that it rendered the payment provision superfluous. Process America Inc. v. Cynergy Holdings LLC, 839 F.3d 125, 137 (2d Cir. 2016). Under the agreement, Process America sold Cynergy's bankcard services and received residual payments as compensation.

Process America sued for improperly withheld residual payments. The contract limited Cynergy's total cumulative liability to fees derived during the last four months of the agreement, except for liability arising from gross negligence, recklessness, or willful misconduct. The trial court granted summary judgment to Process America but limited damages under the clause to four months of fees.

The party who did not promptly enforce payment obligations was barred from pursuing residuals more than four months old.

The court emphasized this was "the contract that the parties bargained for" and that New York courts routinely enforce such provisions between sophisticated parties. Id. Additionally, there must be more than a "simple breach of contract" to disregard the clause—specifically, a showing of "intent to inflict harm."

In Powermat Technologies, Ltd. v. Belkin International Inc., the court even applied a limitation of liability to cap damages for unpaid royalties. Powermat Technologies, Ltd. v. Belkin International Inc., No. 19-CV-878 (VSB), 2020 WL 2892385 (S.D.N.Y. Apr. 2, 2020). Under a license agreement, Powermat provided Belkin a license to use its patents in exchange for quarterly royalty payments.

When Powermat discovered unpaid royalties, it sued for breach. Belkin moved to cap Powermat's recovery under the agreement's limitation of liability provision, which excluded indirect, incidental, consequential, special, or punitive damages and capped each party's total liability at fees paid in the twelve months preceding the claim.

The court enforced the provision, noting that the royalty provisions "address the parties' substantive rights and obligations in the normal course of business," while the limitation of liability "addresses damages in the event of a legal dispute." The court added that even if the agreement "created undesirable incentives for Belkin [not to pay royalties], it is nevertheless 'the contract that the parties bargained for'."

The Consequences of Unclear Drafting

It is not just parties seeking to avoid broad limitation clauses who must be careful. These clauses also contain traps for the unwary party who includes strict limitations intending to rely on them.

Limitation of liability clauses are strictly construed against the party seeking to avoid liability. Terminal Cent., Inc. v. Henry Modell & Co., Inc., 212 A.D.2d 213, 219 (1st Dep't 1995).

This rule—often referred to by its Latin translation contra proferentem ("against the person bringing it forward")—is one of general application. Contract clauses specifying that no one party should be considered the draftsman will not avoid its application.

Under New York law, a limitation of liability clause must be unambiguous, explicit, and clear to be enforceable. Terminal Cent., Inc. v. Henry Modell & Co., Inc., 212 A.D.2d 213, 218-19 (1st Dep't 1995); PRO Net, LLC v. ACC TeleCom Corp., 294 A.D.2d 857 (4th Dep't 2002); 1861 Cap. Master Fund, LP v. Wachovia Cap. Markets, LLC, 95 A.D.3d 620, 621 (2012). Courts scrutinize such clauses, and if found ambiguous, may render the entire provision unenforceable. Placing the provision in bold text and/or capital letters under a heading clearly labelled "LIMITATION OF LIABILITY" is advisable to help establish that it was explicit and clear. Whether a clause is ambiguous or not depends on its precise wording, as explained in the section above.

The cases above focused on strict enforcement of limitation clauses. But many other cases involve parties unable to enforce the limitations they believed protected them. Careful drafting—and careful consideration of how the clause will operate in each possible factual scenario—is the best way to ensure a clause is mutually understood and enforceable.

Courts typically rule on ambiguity at the summary judgment phase, with three possible outcomes: (1) the clause is unambiguous and enforceable, avoiding trial; (2) the clause is unambiguous and enforceable, but other disputed issues require trial; or (3) the clause is ambiguous and therefore unenforceable.

Ironically, ambiguities in limitation of liability clauses cause a provision designed to allocate risk to become the source of uncertainty as to who accepted those risks—forcing the parties to resort to further negotiation or litigation.

What To Be Aware Of

Parties and counsel negotiating limitation of liability clauses should closely consider the legal and commercial impacts of the language used.

As the cases above demonstrate, courts enforce these provisions as drafted, even when they create undesirable incentives. When drafting, it is essential that you:

· Keep the language explicit and clear. If you can't explain it, re-draft it;
· Play out all outcomes before execution, including in particular the most unfavorable outcomes in which one party simply refuses to perform, and adjust the limitation of liability clause as necessary to protect yourself from that outcome;
· Do not use a template without sufficient customization;
· Do not tie the provision to the contract price, instead allowing separate specific representations and warranties about the quality of the goods or services to be provided be the mechanism for ensuring that what is being promised will get delivered and paid for;
· Do not take a "one size fits all" approach—consider each party's exposure and customize appropriately to that exposure.

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