

Whitepaper Conference

What is the current judicial thinking on indirect and consequential loss clauses following the spate of recent legal cases?

Finola McCarthy, Partner

Tuesday, 27 September 2022

Today's Speaker



Finola McCarthy

RDJ LLP

Partner

E finola.mccarthy@rdj.ie

T +353 21 4802771

Agenda

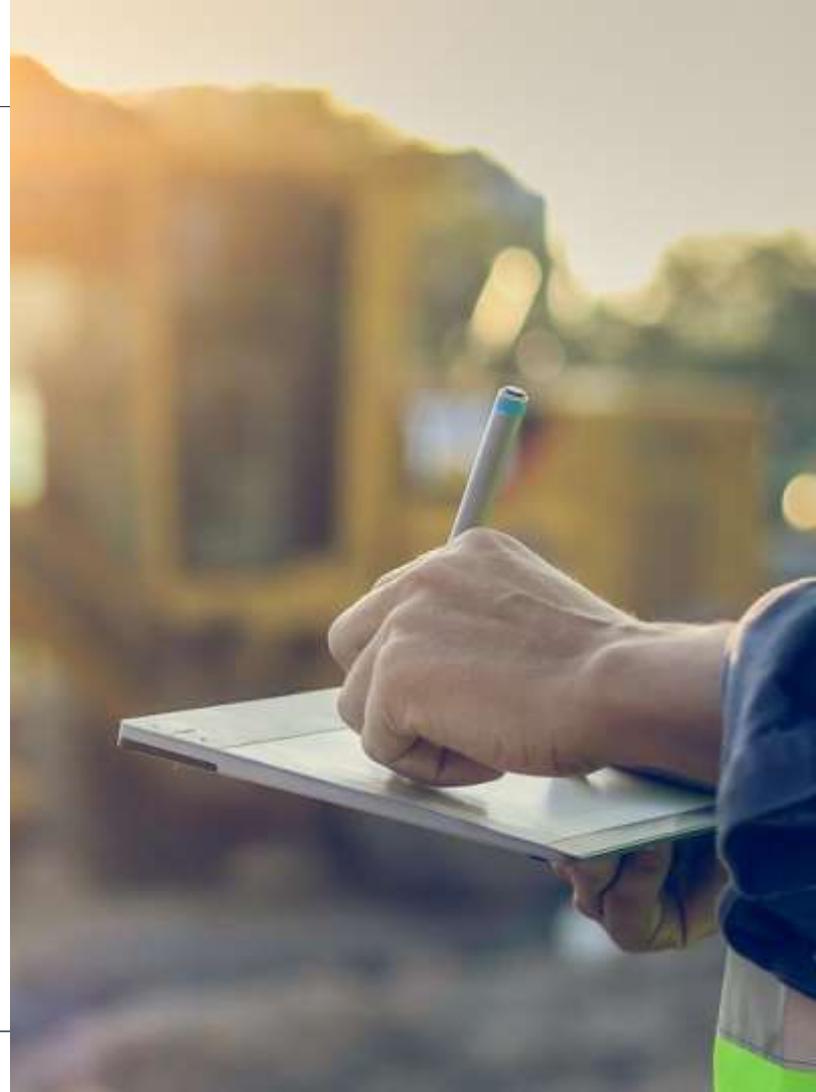
Indirect and Consequential loss clauses

What are they?

Why are they important?

What is changing?

Key Takeaways



Indirect and Consequential loss clauses

Sample clause - FIDIC Red Book, Clause 17.6

“Neither party shall be liable to the other Party for loss of use of any Works, loss of profit, loss of any contract or for any indirect or consequential loss or damage which may be suffered by the other Party in connection with the Contract, other than under Sub-Clause 16.4 [Payment on Termination] and Sub-Clause 17.1 [Indemnities].”

- What is **consequential loss**?
- What is **indirect loss**?

Recap - Rule in Hadley v Baxendale (1854)

“Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either

- arising naturally, i.e. according to the usual course of things from such breach of contract itself, or*
- such as may reasonably be supposed to have been in the contemplation of both parties at the time they made the contract, as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under those special circumstances so known and communicated”*

Direct Loss	Indirect Loss
Economic Loss	Remoteness of damages

Interpretation of consequential and indirect

- Courts take the view that consequential and indirect = second limb of Hadley v Baxendale

Clause in supply contract:

Supplier is “not under any circumstances to be liable for any consequential loss or damage caused or arising by reason of late supply..”

(Croudace Construction Ltd v Cawoods Concrete Products Ltd 1978)

“Neither the Supplier nor the Purchaser shall bear any liability to the other for loss of production, loss of profits, loss of business or any other indirect losses or consequential damages arising during and/or as a result of the performance or non-performance of this contract.”

“Neither party will be liable to the other for any indirect or consequential loss, (both of which include, without limitation, pure economic loss, loss of profit, loss of business, depletion of goodwill and like loss).”

(BHP Petroleum Ltd v British Steel Plc [1999] 2 All ER (Comm) 544.)

(Polypearl Ltd v E.On Energy Solutions Ltd [2014] EWHC 3045 (QB).)

What is changing (1)

Courts willing to look at the ordinary meaning of the words in their particular context

- interpretation is the ascertainment of the meaning which a document would convey to a reasonable person having all the background knowledge which would reasonably be available to the parties in the situation in which they were at the time. The meaning of the document is not the same thing as the meaning of its words

Law Society v MIBI [2017] IESC 31 (adopted the views of Lord Hoffman in *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 All ER 98)

Recent cases

- **Transocean Drilling UK Ltd v Providence Resources plc** [2016] EWCA Civ 372
- **Star Polaris LLC v HHIC-PHIL Inc** [2016] EWHC 2941
- **2 Entertain Video Ltd v Sony DADC Europe Ltd** [2020] EWHC 972

What is changing (1)

Transocean Drilling UK Ltd v Providence Resources plc

[2016] EWCA Civ 372

- Drilling rig defect
- Caused delay
- Hirer sought to recover spread costs- wasted costs of third party equipment and services
- Clause 20 defined consequential losses as
 - (i) any indirect or consequential loss or damages under English law and/or
 - (ii) to the extent not covered by (i) above, loss or deferment of production, loss of product, loss of use... loss of business and business interruption, loss of revenue... loss of profit or anticipated profit...”

The language of cl.20 was clear and excluded liability for wasted costs in the form of the spread costs which the hirer sought to recover.

The principle of freedom of contract required the court to give effect to the parties' agreement



What is changing (2)

Star Polaris LLC v HHIC-PHIL Inc [2016] EWHC 2941

- Ship built by Defendant
- Suffered serious engine failure within 6 months of delivery
- Owner claimed costs of repair, towage fees to Korean port, various related expenses and diminution of value
- Shipbuilder agreed to repair and pay for physical damage



What is changing (2 (cont'd))

Clause IX

4. Extent of BUILDER's Liability

*(a) After delivery of the VESSEL the responsibility of the BUILDER in respect of or in connection with the VESSEL or this CONTRACT shall be limited to the extent expressly provided in the Paragraph 4 of this Article. **Except as expressly provided in this Paragraph, in no circumstances and on no ground whatsoever shall the BUILDER have any responsibility or liability whatsoever or howsoever arising in respect of or in connection with the VESSEL or this CONTRACT after the delivery of the VESSEL. Further, but without in any way limiting the generality of the foregoing, the BUILDER shall have no liability or responsibility whatsoever or howsoever arising for or in connection with any consequential or special losses, damages or expenses unless otherwise stated herein.** Any liability to any third party or any fine, compensation, penalty or other payment or sanction incurred by or imposed upon the Buyer or any other party whatsoever in relation to or in connection with this CONTRACT or the VESSEL until the delivery and acceptance of the VESSEL shall be burdened with the BUILDER (emphasis added)*

What is changing (2 (cont'd))

Court looked at 2 questions of law

- i. What is the correct construction of the phrase "consequential or special losses, damages or expenses". In particular, does that phrase mean such losses, damages or expenses as fall within the second limb of *Hadley v Baxendale* (1854) 9 Ex 341 ? Alternatively, does the phrase have a "cause and effect" meaning, as held by the Tribunal?
- ii. If the Tribunal is right as to the meaning of "consequential or special losses, damages or expenses", on a proper construction of Article IX(4)(a), does diminution in value constitute a "consequential or special loss"?

Held

- "consequential or special losses, damages or expenses" does not mean such losses, damages or expenses as fall within the second limb of *Hadley v Baxendale* but does have the wider meaning of financial losses caused by guaranteed defects, above and beyond the cost of replacement and repair of physical damage.
- by excluding liability for consequential or special losses, damages or expenses", the parties intended to exclude all financial losses, consequent on physical damage that had not expressly been accepted. The obligation is only to replace or repair and is exhaustive.

What is changing (3)

2 **Entertain Video Ltd v Sony DADC Europe Ltd** [2020] EWHC 972

- Civil disorder and riots in London in 2011
- Fire destroyed Sony's warehouse
- Sony provided logistic services and warehouse storage facilities to 2E who stored stock valued at 40m pounds
- 2 Entertain claimed loss of profit and other business interruption losses against Sony
- Exclusion clause in the contract
“Neither party shall be liable under this Agreement in connection with the supply of or failure to supply the Logistics Services for any indirect or consequential loss or damage including (to the extent only that such are indirect or consequential loss or damage only) but not limited to loss of profits, loss of sales, loss of revenue, damage to reputation, loss or waste of management or staff time or interruption of business”.



What is changing (3 (cont'd))

- Court looked at the ordinary and natural meaning of the clause.
- Clause could not be interpreted to exclude the loss of profits and business interruption costs claimed by 2E.
- These losses flowed directly and naturally from the fire and from Sony's breach in failing to provide the services.

Key Takeaways

- Most losses are direct losses because they are the normal results of a breach
 - Most financial or economic losses are direct losses
 - Don't assume that by excluding indirect and consequential loss, you have limited your liability for financial or economic loss
 - Consider the types of losses you want to exclude
- List identified, defined categories of loss in the clause e.g.
 - wasted management time;
 - loss of production,
 - business, or expectation;
 - the cost of getting items from another source
- Or/**
- Accept liability for all losses, whether direct or indirect, but subject to a financial cap.

www.rdj.ie
info@rdj.ie

twitter.com/RDJ_LLJ
[linkedin.com/company/rdj-llp](https://www.linkedin.com/company/rdj-llp)

**Thank you for your time.
Any questions?**

RDJ

**Legal Insight
Human Intelligence
Business Impact**