

# Interpreting Limits on Liability

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# Background

- Exclusions, limitations, caps and indemnities
- Disclaimer: this is not a comparative law analysis, a survey on market practice or a drafting workshop
- 6 ideas in 20 minutes

# Agenda

- Direct v Indirect
- The meaning of consequential loss
- The exclusion of consequential loss
- Loss of profit
- Rules of construction
- Indemnities

# Interpretation of exclusion clauses

- “...*the interpretation of an exclusion clause is to be determined by **construing the clause according to its natural and ordinary meaning, read in the light of the contract as a whole, thereby giving due weight to the context** in which the clause appears including the nature and object of the contract, and, where, where appropriate, construing the clause contra proferentem in a case of ambiguity...*” (emphasis added)

*Darlington Futures Ltd v Delco Australia Pty Ltd (1986) 161 CLR*

# Hadley v Baxendale

- Two limbs:
  - damages which are according to the usual course of things or which directly and naturally flow from the breach (**the first limb**)
  - damages which may reasonably be supposed to have been in the contemplation of the parties at the time they made the contract as a probable result of its breach (**the second limb**)
- Rule deals with remoteness of damage (i.e. it grades losses according to the contemplation of the parties)

# Direct and indirect loss

Direct	Indirect
Costs of obtaining replacement services	Unique economic loss
Costs incurred in replacing faulty equipment	Production shortfall
Temporary bypass/ workaround costs	Loss of anticipated saving
Difference in value of goods at time for delivery and actual delivery.	Loss of reputation and goodwill
Fees paid for services not properly performed.	Reduction of business value

# Consequential loss

- The terms “indirect”, “special” and “consequential” are used interchangeably
- *Croudace Construction Ltd v Cawoods Concrete Products Ltd* [1978] Lloyds Rep 55
  - “consequential loss” means loss recoverable under the second limb of *Hadley v Baxendale*
- So...
  - “consequential” means “special” in the sense that it is unusual
  - consequential loss exclusion won’t limit liability for 1<sup>st</sup> limb
  - rules of remoteness used to interpret a term arguably understood to address “causation”

# Environmental Systems P/L v Peerless Holdings P/L [2008] VSLA 26

- Distinguish between:
  - “normal loss” which is the loss that every plaintiff in a like situation will suffer; and
  - “consequential loss” which is anything beyond the normal measure, such as profits lost or expenses incurred through the breach
- *Allianz Australia Insurance Ltd v Waterbrook at Yowie Bay* [2009] NSWCA 224
- *Alstom v Yokogawa Australia* (No 7) [2012] SASC 49
- So... “consequential” means anything beyond (or other than) the normal or conventional measure of damages



## Peerless (2)

- Encapsulates McGregor’s distinction between “normal” v “special” and claims the mantle of “natural and ordinary” meaning
- But...
  - what is the “normal” measure
  - why use a rule for the measurement of damages to interpret “consequential”
  - why automatically exclude all lost profits or expenses
- *“The words [indirect or consequential] must be given their ordinary and natural meaning. In those circumstances, any loss consequential or following, immediate or eventual, flowing from a breach of contract... is excluded from recovery...”*

*Alston v Yokogawa Australia* [No 7] [2012] SASC 49

# *Regional Power Corporation v Pacific Hydro Group Two P/L [No 2] [2013] WASC 356*

- In 1994 Pacific Hydro agreed to construct Ord Hydro Power Station and then supply electricity from it to Regional Power
- In 2006, an outage occurred and it was inoperable for two months
- Regional Power claimed damages for:
  - diesel generation at Kunanurra Power Station
  - salary and travel for employees to Kunanurra Power Station
  - equipment needed at Kunanurra Power Station
  - diesel fuel

## Regional Power (2)

- *“Neither the Project Entity nor SECWA shall be liable to the other party in contract, tort, warranty, strict liability, or any other legal theory for any indirect, consequential, incidental, punitive or exemplary damages or loss of profits”*

## Regional Power (3)

- *“To reject the rigid construction approach towards the term “consequential loss” predicated upon a conceptual inappropriateness of invoking the Hadley v Baxendale dichotomy as to remoteness of loss, only then to replace that approach by a rigid touchstone of the “normal measure of damages” and which always automatically eliminates profits lost and expenses incurred, would pose equivalent conceptual difficulties.”*

Martin J

## Regional Power (4)

- *“...At its widest, the word “consequential” might always be read as being somehow responsive to something, and thereby encapsulating almost every economic outlay, following upon a breach. But that is not a sensible meaning to attribute to the word “consequential”...”*

*Martin J*

- *“...I regard consequential loss as confined to that loss which GEC might incur as a result of using or being unable to use its plant or capital investment for a purpose extraneous to that directly contemplated by the transaction documents...”*

*Ryan J*

*GEC Alstom Australia Ltd v City of Sunshine – unreported 1996*

# Consequential Loss-Summary

- Indirect loss – Croudace
- Anything other than normal loss – Peerless
- No predisposition to the meaning of the term –  
Regional Power
- No High Court authority

## Exclusion of Consequential Loss (1)

### The 'Hadley v Baxendale' approach

"Indirect or Consequential Loss" means any loss that would reasonably have been in the contemplation or was actually in the contemplation of the parties at the time this Agreement was entered into because of specific knowledge relating to the circumstances relating to this Agreement but which does not otherwise flow naturally from the breach.

## Exclusion of Consequential Loss (2)

### The 'Definition' approach

**"Indirect or Consequential Loss"** means any of the following types of losses:

- loss of revenue
- loss of actual or anticipated savings
- loss of profit
- loss of goodwill
- lost opportunity
- any exemplary, punitive or special damage
- any other indirect or consequential losses



## Exclusion of Consequential Loss (3)

### The 'Exclusions to Exclusions' approach

To the full extent permitted at law, Supplier is not liable for [list of excluded heads] or any indirect or consequential loss which, for the purposes of this exclusion, does not include the following losses or expenses:

- management time expended due to the breach
- cost of re-tendering
- costs of obtaining alternate services to the extent that such cost exceeds the amount that would have been payable to the Supplier
- cost of implementing remedial measures to work-around or compensate for the failure

# Loss of Profits

- Typically “indirect” loss but some times “direct loss”
- Merit in specific treatment
- Loss of revenue v loss of profit

# Rules of Construction

- Contra proferentum rule
- Exclusion of liability for negligence
- Repudiation or termination for fundamental breach
- Fraudulent misrepresentations which induce the other party to enter into the contract
- Third parties

# Indemnities

- Construed strictly and any ambiguity resolved in favour of indemnifier - *Andor Transport v Brambles* 2004
- Remoteness
- Mitigation
- Statute of Limitations