Consequential Loss? In a Sense No Loss Is Consequential

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In this article I review the long-vexed issue of the meaning of 'consequential' as a term in exclusion clauses, critiquing the jurisprudence of the High Court and the Court of Appeal in England and Wales. In a detailed review of doctrine, empirical study, and drawing on experience, I demonstrate that courts get grammar wrong, misunderstand the limb one/limb two *Hadley v Baxendale* divisor and ascribe clearly remote losses to limb one. I argue that they ignore important comment from the House of Lords and Supreme Court. I show that the commercial meaning of 'consequential', supported by eminent textbooks and empirical evidence, which is what parties intend, is ignored by courts which treat the term as if 'consequential' connotes causation whereas commercial players use it in the sense of a genus or type of loss. I suggest practical drafting and hazard a default description of 'consequential' as a commercial/legal term.

Introduction

When a trial court in England or Wales (or the Court of Appeal) is confronted 1
with a contractual term which seems to seek to exclude 'consequential' loss or damage, or 'indirect or consequential' loss or damage, in almost every case the court does the following:

- It conflates 'consequential' with 'indirect'. It says 'consequential' means indirect or not direct, even where the term in question reads 'indirect or consequential'.
- It divides loss into direct and indirect, usually asserting that this is the *Hadley v Baxendale*[1] dividing line.
- It assesses the nature of the losses in dispute and, by way of what is a tacit irrebuttable presumption, places them all into the 'direct' category, conflating limb one with 'direct', proclaiming that none is consequential or indirect, no matter how esoteric the loss and no matter how clear it is that the loss is a limb two loss, in some cases going so far as to classify

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1 (1854) 9 Ex 341; 156 ER 145.

losses which appear to be clearly remote (therefore beyond limb two) as direct.

2 Each step involves an error of logic, grammar or law (sometimes all three). Courts take a dogmatic approach, ignoring precedent and advice from the House of Lords, the Supreme Court and eminent textbook writers, in the process denuding the term 'consequential' of meaning and signally, sometimes expressly, failing to consider the likely intention of the parties.

3 Professor Carter argues that where a contract party seeks to exclude 'consequential loss' the courts, at least in England and Wales, may have pinned a fixed meaning on the word 'consequential'.[2] This article disagrees, arguing that what the courts, in particular in England and Wales, have done is to remove any ascertainable or stable meaning from the word 'consequential'.[3] If there is a definition it is negative, that 'consequential' means 'not direct' or 'indirect' (even where the exclusion is of, for example, consequential and indirect loss) with an illogical and silent corollary that no damage is indirect.

4 Unlimited contractual liability under commercial contracts may reach multiples of the contract price and businesspeople are obviously and rightly nervous of such existential liabilities. For example, in *British Sugar v NEI Power Projects Ltd* (*British Sugar),*[4] NEI had limited its liability for 'consequential loss' to the contract value. There were repeated problems with switchgear acquired for around £100,000 and British Sugar sued NEI for over £8,000,000 in respect of loss of profits, loss of production, loss of electrical generation profits, and additional maintenance costs. In *Pegler Ltd v Wang (UK) Ltd,*[5] Pegler claimed more than £22,000,000 on a contract valued at £1.2M, lawyers involved commenting in a blog that:[6]

> Possibly the most significant fact about this judgment does not appear in the judgment at all: it is that Wang went into voluntary liquidation shortly after the judgment was given, blaming the amount awarded as the cause.

5 West provides a US example of a construction manager contracted to provide services for a fee of $600K having damages of $14.5M awarded

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2 J W Carter, 'Exclusion of Liability for Consequential Loss' (2009) 25 *JCL* 118 at 118 citing Fry J's claim in *Holt v Collyer* (1881) 16 Ch 718 at 722 that words (in this case the word used in a lease being 'beerhouse') might have fixed meanings, Carter arguing that in contract meaning varies with context.

3 See Glenn D West, 'Consequential Damages Redux: An Updated Study of the Ubiquitous and Problematic "Excluded Losses" Provision in Private Company Acquisition Agreements' (2015) 70 *The Business Lawyer* 971 at 993: 'The losses excluded by … the term "consequential damages" … are simply not easily known or categorised …'.

4 (1997) 87 BLR 42.

5 [2000] BLR 218 *(Pegler v Wang)*.

6 *Pegler v Wang* (Pinsent Masons 2007) Pegler v Wang (pinsentmasons.com). See more recently *Drax Energy Solutions Ltd v Wipro Ltd* [2023] EWHC 1342 (TCC) where the supplier was faced with a claim for over £31M on a contract value of £7.6M.

against them, saying that the award appears to have resulted in amendment of the standard form of contract in the industry.[7]

I spent a lifetime, a commercial lifetime, in analysing, drafting, advising 6
on, negotiating, 'value engineering', and managing contracts, including dispute management (sometimes creating the dispute!). Almost all was spent in the provision or purchase of complex equipment, systems or controls. In such contracts, as in many other commercial contracts, including IT systems and service contracts, facilities management and outsourcing contracts, the underlying, well-recognised purpose of the deal is either to save money or make money, whether this is, for example, by generating power, providing propulsion power for ships, carrying and transferring bulk products such as urea or cement, providing hydraulic power to bridges or lock gates or mine-winders, compressing boil-off gases in LNG plants, or speeding up airport bag transfers (sometimes supporting new electronic security bag checking systems), weapons and stores handling for naval vessels,[8] or keeping power stations going by supplying them with coal, oil or nuclear fuel, or off-taking ash or used nuclear fuel rods. The risk which keeps businesspeople awake at night in such contracts is that of 'consequential' loss, a portmanteau term whose natural commercial meaning, I say, plainly covers generally uninsurable financial and economic loss such as loss of profit, loss of use, or loss of production. The risk is, as we shall see from the cases, clearly considerably higher for the supplier, including feedstock suppliers, but one can envisage cases where there might be a similar risk to a client.[9] I will return to this later but my argument is that the word 'consequential' is normally intended to cover this *type or genus* of damage or loss.[10]

In this article I look at the issue in three parts. In the first I discuss the 7
conflation of 'consequential' with 'indirect' and the even more eccentric refusal to agree that 'indirect and consequential' might mean something different to 'consequential'. In the second section, using as my thread the key loss of profit cases, I examine whether the limb one/limb two dividing line can be described as direct v indirect; it can't. In the third section I examine the trial treatment of claimed damages, finding that in almost every case damage claimed is classified as direct, and therefore limb one and not consequential, and I consider some of the more esoteric losses claimed and recovered, asking whether it is credible to place them into limb two.

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7 West, above, n 3 at 984.

8 There is a loss of use risk in these contracts. See eg *The Chekiang* [1926] AC 637.

9 Alfred A Hudson, *Hudson's Building and Engineering Contracts,* Nicolas Dennys and Robert Clay, eds, 13th ed, Sweet & Maxwell, London, 2015, cites many contractor's claims at pp 6–15, and these claims do not tend to approach contract values. Loss of profit claims tend to be the gross profit lost on the instant contract.

10 A point I made at a Kuala Lumpur conference in 2012: C Haward Soper, 'Consequential Loss — What Is It?' (Advanced Contract Risk Management in Oil and Gas) — 'Judges interpret the word "consequential" with reference to causation or remoteness … Commercial people think about the type of loss … '.

Consequential ≠ Indirect

8 I opened the relevant chapter in my ancient MPhil, with these words:[11]

> It is often thought, particularly in the mechanical and electrical engineering industry, that the phrase 'consequential loss' is a cover all for any 'metaphysical' or 'economic' loss such as lost profit or production …

9 The first case in which a clause seeking to exclude 'consequential' loss was considered seems to have been in 1935 in *Millar's Machinery Co Ltd v David Way & Son (Millar's)*.[12] At first instance Maugham J (later Maugham LC in Neville Chamberlain's government), found that losses such as the costs of a machine to replace a rejected gravel washer and associated expenses (such as the lost cost of erecting the rejected machine and the difference in price between that and the replacement) were direct and not consequential. This is a sensible commercial analysis. Any reasonable supplier would accept that they should accept liability for those costs.

10 Although there is no evidence in the case law (I ran a Lexis search for pre-1935 mentions of 'consequential' in an exclusion clause, finding none) for Maugham J's claim that consequential 'has come' to mean 'not direct', there are contemporaneous pointers to what was considered direct and what consequential, including one case in which he was empanelled. In the House of Lords, in a charterparty case, *Rendal A/S v Arcos Ltd,*[13] a claim was made for delay, loss of time and consequent expenses. Lord Wright, with Lord Maugham on the bench, clearly differentiated between physical damage to the hull and 'the consequential loss and expense'.[14] In a later case Lord Radcliffe makes a similar observation, discussing 'consequential damage: such, for instance, as a loss of business at the dock or harbour'.[15] It is also worth remembering that Parke B, in 1841, referred to loss beyond

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11 C Haward Soper, 'Some Issues in Contemplation and Damages in the Common Law of Contract' (University of Leicester 1992) at G1. See also Alfred A Hudson and I N Duncan Wallace, *Hudson's Building and Engineering Contracts,* Sweet & Maxwell, London, 1970, pp 597–8, listing such losses as consequential, and Terence Daintith and Geoffrey Willoughby, *A Manual of United Kingdom Oil and Gas Law,* Oyez, London, 1981, cited below. See also G C Cheshire, C H S Fifoot and M P Furmston, *Cheshire, Fifoot and Furmston's Law of Contract,* 11th ed, Butterworths, London, 1986, p 587 who refer to losses occasioned by the falling price of sugar in Basrah as 'consequential' and limb two — in *Koufos v C Czarnikow Ltd (The Heron II)* [1969] 1 AC 350.

12 (1935) 40 Com Cas 204, Millar's being a leading manufacturer of road-making plant and contracting machinery: 1930 *Industrial Britain: Millars' Machinery Co — Graces Guide*.

13 [1937] 3 All ER 577.

14 [1937] 3 All ER 577 at 586–7. See also *Stonedale No 1 Dumb Barge (Owners) v Manchester Ship Canal Co, The Stonedale No 1* [1954] P 338 at 352 (affirmed [1956] AC 1); Singleton LJ refers to damage '… confined to that physically caused to the harbour works and does not include consequential loss of revenue through inability to use the harbour'.

15 *Workington Harbour and Dock Board v Towerfield (Owners)* [1951] AC 112 at 161 per Lord Radcliffe. See also *Cox v S Cutler & Sons Ltd* [1948] 2 All ER 665 at 669 where consequential is so described, albeit this is a tort case.

'the difference between the price contracted for and the real value of the articles …' as 'consequential'.[16]

Maugham J seems not to have had much evidence and no precedent to back up his claim that consequential 'has come to' mean not direct but Atkinson J in *Saint Line Ltd v Richardsons, Westgarth & Co Ltd*[17] *(Saint Line)* delved deeply into both *Webster's New International Dictionary* and the *Oxford English Dictionary* (OED). 'Consequential' according to both carries two main meanings, one being 'Of the nature of a consequence or sequel; following esp. as an effect or result' and the OED's second meaning is 'Of the nature of a consequence merely, not direct or immediate'.[18] The second definition in the 1928 *Webster's New International Dictionary* is almost identical but cites as 'Law' limb two damages as being consequential.[19] Oddly, the OED citation for the second meaning contains a 19th-century US legal quotation from Wharton's 19th-century digest.[20] The third definition is 'Following; as an inference or conclusion'. The fifth OED meaning (obsolete according to the OED, but not according to me) is 'Pregnant with consequences … important' which resounds in Webster's third definition (not obsolete according to Noah) as '… of consequence, important, weighty'.[21] I was tempted to concoct an easy-to-strangle argument that this is what businesspeople mean by consequential but it seems to me to be as unproductive to make that case as it is to make the meaning one case; that all damage is consequential.[22] Limb two is an easier case to make despite the defect that the limb one/limb two dividing line is not congruent with direct/indirect. The fact that there are several meanings in each dictionary should alert judges to the possibility that context is important in this search for meaning, Chitty making the point that the ordinary and natural meaning is 'not necessarily the dictionary meaning of the word'.[23] 11

McGregor cites various cases as showing that in tort 'consequential' means loss beyond the 'normal measure',[24] and is surely right to question the dichotomous use of 'consequential' in tort and contract saying that 'the 12

16 *Mondel v Steel* (1841) 8 M & W 858; 151 ER 1288 at 1293. Cited by J Edelman, ed, *McGregor on Damages,* 21st ed, Sweet & Maxwell, London, 2020, para 3-013.

17 [1940] 2 KB 99.

18 Carter, above, n 2, makes this point at 124–5.

19 Noah Webster and William Torrey Harris, *Webster's New International Dictionary of the English Language*, G Bell and Sons, Ltd, London, 1928.

20 Thomas Isaac Wharton, *A Digest of the Reported Cases Adjudged in the Several Courts Held in Pennsylvania; together with Some Manuscript Cases,* 2nd ed, Philadelphia, 1829, also cited by Atkinson J in *Saint Line* [1940] 2 KB 99 at 104.

21 In fact the word is used thus in contemporaneous usage. Two newspapers use it in headlines on the subject of Boris Johnson — see D Frost, 'Boris Johnson Was One of the Most Consequential Politicians in Decades', *Sunday Telegraph*, London, 10 June, and G Brandis, 'Love Him or Loathe Him, Boris Johnson Was Britain's Most Consequential PM since Thatcher', *Sydney Morning Herald*, 7 July 2022.

22 *Saint Line Ltd v Richardsons, Westgarth & Co Ltd* [1940] 2 KB 99 at 105.

23 *Chitty on Contracts,* Hugh Beale, ed, 34th ed, Sweet & Maxwell, London, 2021, para 15-063.

24 McGregor, above, n 16, para 3-013 citing *Workington Harbour and Dock Board v Towerfield (Owners)* [1951] AC 112.

abandonment of the division in contract does not sit well with its retention in tort'.[25] Treitel does not agree with this analysis saying that if parties want to utilise the 'meaning which is given to "consequential loss" in the law of damages generally it is easy to find a form of words to make this happen' but, as we shall see, this is not a good commercial analysis.[26] As Carter says 'commercial parties might be expected to use [consequential loss] in a commercial rather than a legal sense'.[27]

13 The right approach is surely for the court to ask itself how such a 'serious utterance would be interpreted in ordinary life', Lord Hoffmann's phrase.[28] The difficulty with relying on the OED, especially on the first, narrow, definition, as Atkinson J spotted, is that, because 'in a sense all damage is consequential' an exclusion of 'consequential' damage would, as the Court of Appeal in *Croudace Construction Ltd v Cawoods Concrete Products Ltd*[29] *(Croudace)* noted, potentially exclude all damage. If a commercial player wanted to exclude all damage, I suggest, they would say so in terms. That said, that is no reason to suggest, as Atkinson J did, that what was meant was solely the second definition; of indirect/Wharton damage. If a commercial player meant to exclude 'indirect' damage they would, I suggest, do so in terms, which the drafters did in *Saint Line*, only to be ignored with the Court of Appeal in *Croudace* approving Atkinson J's ruling that 'I do not think "consequential" adds anything to the word "indirect"'.

14 The result of *Saint Line* and *Croudace* is that 'consequential' means the same as indirect or consequential, which cannot be right. The drafter appears on the face of it to have been very careful to differentiate 'consequential' and 'indirect' by using 'or'. A normal interpretation would be that the two terms represent something different.[30] It is possible that Atkinson J recognised this argument as his judgment maintains that 'I do not think "consequential" adds anything to the word "indirect"'.[31] The idea that a drafter would say that they seek to exclude indirect or not direct damages and that the two terms are 100 per cent congruent is, frankly, improbable. The same issue arises in future cases and the drafting receives the same treatment in those.[32] It seems to me to be far more likely that the term 'consequential' in *Saint Line* was used by the draftsperson in Lord Wright's commercially comprehensible sense to ensure that liability for uncontrollable economic losses, as well as 'indirect' loss, is excluded.

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25 McGregor, above, n 16, para 3-015.

26 Edwin Peel, *Treitel on the Law of Contract,* 15th ed, Sweet & Maxwell/Thomson Reuters, London, 2020, para 7-011.

27 Carter, above, n 2 at 123.

28 *Investors Compensation Scheme v West Bromwich Building Society* [1998] 1 WLR 896 at 912.

29 [1978] 2 Lloyd's Rep 55; (1978) 8 BLR 20.

30 See however Grant Follett, 'Just What Is "Indirect or Consequential Loss"?' (2004) *Computers and Law* 11, doubting this argument.

31 *Saint Line Ltd v Richardsons, Westgarth & Co Ltd* [1940] 2 KB 99 at 104.

32 See eg *GB Gas Holdings Limited v Accenture (UK) Ltd* [2009] EWHC 2734 (Comm); *Pegler v Wang*; *Hotel Services Ltd v Hilton International Hotels (UK) Ltd* [2000] BLR 235; [2000] EWCA Civ 74 (*Hotel Services*).

15 Indeed, the language of insurance contracting, particularly where the primary risk insured is physical damage, provides major evidence that 'consequential' has not 'come to' mean indirect. There, essentially, the dividing line is a category divisor, with physical loss being explicitly contrasted with consequential loss,[33] Pollock CJ referring to loss of profit as a 'consequential mischief' in an early case.[34] The principles, boiled down, are clear enough. Consequential loss is insurable.[35] Consequential loss, 'most commonly … manifested in the form of loss of profit',[36] is not recoverable unless expressly covered, even such terms as 'all risks' being interpreted as meaning only physical loss.[37]

16 The problem is that in some contract settings we have a category difference between judicial constructs and commercial constructs. Judges take one dictionary meaning (out of several) directed towards causation whereas the commercial player uses a shorthand to describe a genus or class.

Loss of Profit Redux/The Dividing Line

17 In *Saint Line*, the loss of profit claimed by the shipowner was described by Atkinson J as a claim which might 'directly and naturally' arise from delayed delivery. It is not controversial that loss of profit may be direct, or direct and natural, as Lord Herschell made clear in *The Argentino* in 1889.[38] In 1972 both Lords Pearson and Diplock refer to loss of profit as consequential; in a case, however, where nothing turned on that issue.[39] Lord Diplock was clear: 'The employer may have been deprived of the profitable use of the works … Such consequential damage … '.[40]

18 An examination of the key cases on loss of profit shows that the limb one/limb two dividing line, often, usually inferentially, described as direct/indirect in the consequential loss cases, is not between direct and indirect. In *Hadley v Baxendale*, for example, Baron Alderson accepted that the delay

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33 Robert Merkin, ed, *Colinvaux's Law of Insurance,* 13th ed, Sweet and Maxwell, London, 2022, paras 11-222–11-226. See the discussion on business interruption insurance at 24-091 onwards. See also Raoul Colinvaux and Robert Merkin, *Colinvaux's law of Insurance,* 6th ed, Sweet & Maxwell, London 1990, pp 10–19. I acknowledge the assistance of Wayne Courtney on this point.

34 *Theobald v Railway Passengers Assurance Co* (1854) 10 Ex 45; 156 ER 349.

35 *Barclay v Cousins* (1802) 2 East 544; 102 ER 478. It had been thought that such loss might be classed as speculative and therefore uninsurable; see Merkin, above, n 33 at 11-223.

36 Merkin, above, n 33 at 11-223, giving multiple examples at 11-225.

37 *Coven SpA v Hong Kong Chinese Insurance Co* [1999] CLC 223; [1998] EWCA Civ 1573. See also Malcolm A Clarke, *Policies and Perceptions of Insurance: an Introduction to Insurance Law,* Clarendon Press, 1997, para 16 2A-4, citing, however, McGregor's definition of consequential loss.

38 (1889) 14 App Cas 519 at 523: 'loss of earnings which it must reasonably have been anticipated'.

39 *P & M Kaye Ltd v Hosier and Dickinson* [1972] 1 WLR 146 at 160 and 161 per Pearson LJ.

40 *P & M Kaye Ltd v Hosier and Dickinson* [1972] 1 WLR 146 at 165.

to the shaft caused a loss of profit but because this would not happen in the 'great multitude' of cases liability would not arise unless it could be shown to be in the contemplation of the parties; limb two.[41] Similarly in *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd,*[42] loss of profit was a legitimate claim due to Newman's knowledge of the laundry's business: limb two again. And finally in *Koufos v C Czarnikow Ltd* (*The Heron II*)[43] Lord Reid, in a passage which could hardly be more clearly pointing to limb two, ruled:[44]

> In cases like *Hadley v Baxendale* or the present case it is not enough that in fact the plaintiff's loss was directly caused by the defendant's breach of contract. It clearly was so caused in both. The crucial question is whether, on the information available to the defendant when the contract was made, he should, or the reasonable man in his position would, have realised that such loss was sufficiently likely to result from the breach of contract to make it proper to hold that the loss flowed naturally from the breach or that loss of that kind should have been within his contemplation.

19 The dividing line is, therefore, not between direct and indirect, nor between direct and consequential, but rather between:

- direct and natural and in the usual course of things (Lord Reid above) and
- within reasonable contemplation (whether direct or indirect or consequential).

20 Lord Reid's analysis must mean that direct, even direct and natural, is not enough to convey damage into the first limb. The fundamental additional requirement is that it is also damage of a type which would be found in Baron Alderson's great multitude of cases. If it is not, then the limb two question is whether it was or should have been in the reasonable contemplation of the parties. It is clear that 'indirect' loss by definition falls into limb two but not so clear that 'consequential' loss does.[45]

21 There is a second issue in play here which is that where the loss of profit claimed arises from contracts other than the one breached, say a follow-on contract expressly contemplated,[46] or a sub-sale,[47] or an unconnected sale of surplus electricity,[48] it seems well established that such lost profit claims

41 *Hadley v Baxendale* (1854) 9 Ex 341; 156 ER 145 at 151.

42 [1949] 2 KB 528.

43 [1969] 1 AC 350.

44 [1969] 1 AC 350 at 385, noting at 384 that Baron Alderson must have meant by great multitude the 'great majority'.

45 John D Calamari and Joseph M Perillo, *The Law of Contracts,* West Pub Co, St Paul, Minnesota, 1970, p 331: limb two damages are 'frequently known as special or consequential'.

46 See eg *Attorney General of the Virgin Islands v Global Water Associated Ltd* [2021] AC 23; [2020] UKPC 18.

47 *The Heron II*. See the US case *Harper v Wellbeing Genomics Pty Ltd* NO 03-17-00035-CV, (Tex App Dec 4, 2018) — 'profits lost on other contracts or relationships resulting from the breach (such as resale …) are classified as indirect or consequential damages'.

48 *British Sugar* (1997) 87 BLR 42.

generally fall into limb two.[49] The Court of Appeal in *Millar's*, strikingly, disallowed a claim for washed gravel bought by its client David Way to fulfil a future contract in the absence of the contracted for gravel washer as too remote and not in the contemplation of the parties.[50] Benjamin, for example, expressly describes such losses as 'consequential'.[51] West appears to say that this is the general rule in the United States:[52]

> … lost profits are considered general or direct damages when … 'the non-breaching party bargained for such profits and they are "the direct and immediate fruits of the contract",' whereas lost profits are considered consequential damages when they are the result of a 'collateral business arrangement'.

This matters because it helps demonstrate that whether these losses are direct or indirect is not the right question. The right question is whether they were or should have been in the contemplation of the parties. Professor Carter says that the English cases point to a suggestion that 'consequential loss' means loss recoverable only under limb two.[53] One problem with McGregor's analysis that the dividing line is between 'normal loss and consequential loss'[54] is that, for example, loss of profit, which he describes as consequential, and therefore, from his viewpoint 'loss beyond the normal loss', is not abnormal loss,[55] bearing in mind, however, that in *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* Nettle J took the view that loss of profit is 'beyond the normal measure'.[56] In the contracts I dealt with almost all were designed to make or increase profit or save money, so loss of profit may well be, in such cases, limb one, as would loss of use or loss of production. Another is that, even if they are abnormal, they 22

49 See generally J P Benjamin, *Benjamin's Sale of Goods*, 11th ed, Sweet & Maxwell, London, 2021, paras 17-065, 17-067 and 17-076. See also *Elvanite Full Circle Ltd v AMEC Earth & Environmental (UK) Ltd* [2013] EWHC 1191 (TCC). However, see *GEC Marconi Systems Pty Ltd v BHP Information Technology Pty Ltd* (2003) 128 FCR 1; [2003] FCA 50 in which Finn J allocated profits from future electricity supply contracts to limb one.

50 *Millar's* (1935) 40 Com Cas 204 at 209.

51 Benjamin, above, n 49, para 17-037.

52 West, above, n 3 at 991. Stephen Furst and others, *Keating on Construction Contracts*, 11th ed, Sweet & Maxwell, London, 2021, para 9-017, says that such losses are 'likely to *approximate* to loss within the second limb'. See eg *Biotronik AG v Conor Medsystems Ireland Ltd* 22 NY3d 799 at 806 (2014) and *Marley Cooling Tower Co v Caldwell Energy & Envtl, Inc* 280 F Supp 2d 651 at 658–59 (WD Ky 2003).

53 Carter, above, n 2 at 118. The same appears to be true in Singapore — see *Singtel Telecommunication v Starhub Cable Vision Ltd* [2006] 2 SGCA 5.

54 McGregor, above, n 16 at 3-013 and 3-014, for example.

55 McGregor, above, n 16 at 3-013. For a more extended critique of the 'McGregor View' see Carter, above, n 2 at 121 and following. In drafting a Contract Code McGregor proposed that recoverable loss in contract be loss which the party liable 'foresaw or had reason to foresee or could reasonably be regarded as having contracted to be liable', in Harvey McGregor, *Contract Code,* Sweet and Maxwell, Milano: Giuffre Editore 1993, p 437.

56 *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* (2008) 19 VR 358; [2008] VSCA 26 at [93].

are clearly, if I am right that they keep businesspeople awake at night, in the reasonable contemplation of the parties. Lord Reid describes them, as did Baron Alderson, as direct and Atkinson J described them as direct and natural.

23 Returning to the cases, many of the losses classified as direct or limb one do not appear to fit limb one's parameters. Damage, discussed in the following subsection, such as ex gratia payments, lost income from Renewable Obligation Certificates, costs of ongoing microfiching or missed contract sales discounts, seem esoteric and even some way beyond limb two parameters.

Consequential Loss — In a Sense No Loss Is Consequential

24 In 1936 Saint Line, a Liverpool shipping concern whose ships were all named after saints, contracted with the Hartlepool shipbuilder and marine engineer Richardsons Westgarth, a major local employer, for engines capable of developing 800 brake-horsepower at 200 revolutions per minute. They failed on test and were rejected.

25 The contract contained a clause apparently excluding certain liability:

> nor shall their liability ever or in any case … extend to any indirect or consequential damages or claims whatsoever.

26 Richardsons made claims for loss of profit, expenses of wages, stores, etc and fees paid to experts for superintendence, which came before Atkinson J in the form of an Umpire's case stated. His *Saint Line* judgment is remarkable for three reasons.

27 The first is, as discussed above, that he construes the phrase 'indirect or consequential' as meaning indirect or not direct, repeating Maugham LJ's construction of consequential as 'not direct'.[57] In a strikingly odd passage he cites Blackburn J who says that the 'consequences of non-delivery … would be that the purchaser would not be able to earn money by its use, and this loss of profit …', seeming to miss the point that the loss being a consequence must be consequential.[58]

28 The second is that Atkinson J accepts that all damage is 'in a sense' consequential but then does not follow Lord Wright's differentiation between physical loss and consequential loss.[59]

29 Third, what is more remarkable is, as we shall see, that in the future decades of English case law no damage was *ever* found to be consequential. In every case pre-2014 where a court was asked in terms to classify claimed damages, on a bare reading of consequential or indirect and consequential,

57 *Saint Line* [1940] 2 KB 99 at 104.

58 *Saint Line* [1940] 2 KB 99 at 105 citing *Cory v Thames Ironworks Co* (1868) LR 3 QB 181 at 189.

59 In *Rendal A/S v Arcos Ltd* [1937] 3 All ER 577.

the court classified damage as direct.[60] The courts have essentially inverted the logical, etymological position that all damage is consequential with a tacit position that no damage is consequential, except in relatively recent marginal cases.

In the cases of *Wraight Ltd v PH and T Holdings* and *FG Minter Ltd v Welsh Health Technical Services Organisation* a clause providing for the reimbursement of 'Any direct loss and/or damage caused … ' covered interest costs due to late payments and loss of gross profit on the incomplete work.[61] In neither case did the court seem to feel it necessary to allocate the losses to limb one or limb two. 30

In *GKN Centrax Gears v Matbro*,[62] an appeal from an arbitrator's award in the form of a case stated procedure, the Master of the Rolls, Lord Denning, upheld the arbitrator's award of damages for loss of repeat orders, there being an exclusion of 'consequential' loss in a complex and poorly drafted warranty clause, classifying these as limb two. Stephenson LJ, however, placed that damage into limb one.[63] In these cases, where an arbitrator's award is being challenged we should bear in mind the historic reluctance of courts to interfere. 31

Citing *Millar's*, Megaw LJ found, affirming Parker J at first instance, in *Croudace,* that a clause reading 'we are not under any circumstances to be liable for any consequential loss or damage' did not cover losses that began to 'clock up at once' (such as the wasted cost of the workforce, plant and equipment or inflation costs) which were to be regarded as direct, as was a claim from a subcontractor, and the exclusion clause was found to apply solely to limb two losses.[64] The logic of workforce or inflation-driven costs (inflation being more than 8 per cent in 1978) being direct is clear enough but the claim for an indemnity against a subcontractor's claim seems to point to a requirement that such a claim was in the reasonable contemplation of the parties or limb two. 32

In 1998 a court found a way around a valid exclusion of loss of profit by defining wasted overheads as direct loss; although it seems obvious that wasted overheads by definition act so as to reduce profit.[65] In that year the 33

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60 See eg *Star Polaris LLC v HHIC-Phil Inc (The Star Polaris)* [2017] 1 Lloyd's Rep 203; [2016] EWHC 2941 (Comm) (*Star Polaris*)*; Croudace*; *Hotel Services*; *British Sugar*; *Accenture.*

61 *Wraight Limited v PH & T (Holdings) Ltd* (1968) 13 BLR 29 and *FG Minter Ltd v Welsh Health Technical Services Organisation* (1980) 13 BLR 1. See also *Chiemgauer Membran und Zeltbau GmbH (formerly Koch Hightex GmbH) v New Millennium Experience Co Ltd (formerly Millennium Central Ltd) (No 2)* [2000] 12 WLUK 440. See also in Scotland a similar result in respect of loss of profit in *Robertson Group v Amey-Miller (Edinburgh) Joint Venture* [2005] BLR 491; [2005] ScotCS CSIH 89.

62 *GKN Centrax Gears Ltd v Matbro Ltd* [1976] 2 Lloyd's Rep 555 at 573–4.

63 *GKN Centrax Gears Ltd v Matbro Ltd* [1976] 2 Lloyd's Rep 555 at 577.

64 *Croudace*, treated as the key case on this by Robert Ribeiro, *Building and Engineering Contracts: Law and Practice,* Mitchell, London, 1990, p 116. See a similar result in the US in *City of Milford v Coppola Constr Co* 891 A 2d 31 at 40 (Conn App Ct 2006).

65 *Deepak Fertilisers and Petrochemical Corporation v Davy McKee (London) Ltd; ICI Chemicals and Polymers Ltd* [1999] 1 Lloyds Rep 387; [1998] EWCA Civ 1752.

Court of Appeal dealt with a case[66] in which I had an interest, between NEI Power Projects, a former employer, and Alstom, my then-current employer. Waller LJ described the contract: 'The ultimate contract price was about £106,585. The plaintiffs allege that the equipment was poorly designed and badly installed, which resulted in breakdowns in the power supply. The damages claimed are over £5 million, and consist mainly of increased production costs and loss of profits due to breakdowns'. The equipment subcontractor to NEI was Alstom, who had included in their offer a clause in MF/1 form,[67] but NEI had agreed a different limitation with British Sugar to the effect that 'NEI's liability for consequential loss is limited to the value of the contract'. The court held that losses in respect of loss of profits, loss of production, loss of electrical generation profits and additional maintenance costs were not consequential, Waller LJ saying that 'the limitation being imposed in relation to some other type of loss which did not flow so directly, for example, damage which might flow from special circumstances and come within the second limb in *Hadley v Baxendale*'.[68] It is interesting that resale-type profit, from electricity generation, was not considered limb two.

34 In 1999, Bowsher J's judgment in *Pegler v Wang*, an IT case, significantly added to the list of losses which courts consider direct. The total price for the supply of hardware, software, bespoke software programming and services was £1,198,130. Wang faced a claim of £22,898,472. Bowsher J interpreted a clause which runs 'Wang shall not be liable for any indirect special or consequential loss, however arising (including but not limited to loss of anticipated profits or data) …' as excluding liability only for indirect loss of profit and awarded damages under many other heads including the following which seem to be either limb two or even too remote:

- lost sales and loss of ability to increase margins;[69]
- lost opportunity to make staff cost savings;
- £1,463,200 because Pegler could not reduce the cost of purchasing;
- £150,218 paid to third parties for substitute software and consultancy services;
- costs of microfiching and DTP services ;
- contract sales discounts;
- reduction in home trade debtors;
- wasted management time: despite a dearth of written records, Bowsher J

66 *British Sugar* (1997) 87 BLR 42.

67 Institution of Mechanical Engineers, *Model Form of General Conditions of Contract MF/1* (www.imeche.org 2014) ISBN-13: 978-1-84919-804-2. For the wording see the concluding subsection below.

68 *British Sugar*, treated as one of the key cases, alongside *Croudace* by P D V Marsh, *Contracting for Engineering and Construction Projects,* Gower P Institute of Purchasing and Supply, London, 1969, p 29. See also *Syncrude Canada Ltd v Babcock & Wilcox Canada Ltd* (1997) 51 Alta LR (3d) 1 (CA) in which the additional cost of energy consequent on a boiler breakdown was held to be direct.

69 In the US such losses were held to be consequential in *Creighton Univ v Gen Elec Co* 636 F Supp 2d 940 at 943 (D Neb 2009).

adoptied a 'broad-brush' approach, awarding £534,000, half of Pegler's claim.[70]

Hotel Services[71] installed 'Robobars' in Hilton hotels in 1991, the contract providing that Hotel Services would not 'in any circumstance be liable for any indirect or consequential loss, damage or liability from any defect or failure in the System or any part thereof or the performance of this Agreement or any breach hereof…'. One problem was that they emitted ammonia — not a typical Hilton experience. In an entertaining comment Sedley LJ observed:[72] 35

> In the minibar, to be found in many hotel bedrooms, unimagined problems lurk. The honesty bar, which relies on guests accounting for what they have used, generates forms of dishonesty ranging from leaving without paying to refilling bottles with water or other similarly coloured fluids. One answer to this was the Robobar…

In 1995 Hilton Hotels removed and replaced the defective Robobars and sued Hotel Services for the cost of removal (£127K) and loss of profit (£151K), and the court held, predictably and correctly, that the cost of removal was a direct loss and, less obviously, so was the loss of profit. The court approached the question by considering whether there was some special 'mutually known fact', that is, a limb two liability, that established the loss, and if not (and the loss passed the test of remoteness) whether the loss was not 'indirect or consequential'.[73] Sedley LJ did, however, hazard that some loss might (might) be consequential:[74] 36

> An example of consequential loss might be injury to the profitability of the hotel itself [as opposed to the 'thing itself'].

He lamented that he was unable '… to restore to the word "consequential" the natural meaning of which commercial and legal usage in exclusion clauses has long since robbed it'.[75] 37

In 2002, the House of Lords returned, 67 years after *Millar's* and 65 years after *Rendal,* to the definition of 'consequential', unfortunately providing only clues or guidance. In *Caledonia North Sea Ltd v British Telecommunications Plc,*[76] Lord Bingham cited with approval the following 38

70 Which appears to contradict *Tate & Lyle Food and Distribution Ltd v Greater London Council* [1981] 3 All ER 716 in which Forbes J made it clear at 721 that such damages should be a matter of record refusing to 'advance into an area of pure speculation' pointing out that modern office arrangements permit the recording of time spent on managerial matters. The issue of liability and damage in the case came before the House of Lords, *sub nom Tate & Lyle Industries Ltd v Greater London Council* [1983] 2 AC 509, but the question of managerial costs disallowed by Forbes J owing to the failure by Tate and Lyle to record such costs was not part of this appeal.

71 *Hotel Services* [2000] BLR 235; [2000] EWCA Civ 74.

72 *Hotel Services* [2000] BLR 235; [2000] EWCA Civ 74 at [1].

73 *Hotel Services Ltd* [2000] BLR 235; [2000] EWCA Civ 74.

74 *Hotel Services* [2000] BLR 235; [2000] EWCA Civ 74 at [13].

75 *Hotel Services* [2000] BLR 235; [2000] EWCA Civ 74 at [11].

76 [2002] 1 All ER (Comm) 321; [2002] UKHL 4.

passage from Daintith and Willoughby's *Manual of United Kingdom Oil and Gas Law*:[77]

> It will, however, normally be provided that neither the contractor nor the operator will be liable to the other for loss of use of the other's property or any loss of profit or other consequential loss of the other.[78]

39 It seems unlikely that description of loss of profit or loss of use as consequential was accidental (see also Hudson) and Professor Daintith and Geoffrey Willoughby were almost certainly using the term in its natural, commercial sense. Lord Hoffmann made a stronger point:[79]

> I would wish to reserve the question of whether, in the context of the contracts in the *Hotel Services* and similar cases, the construction adopted by the Court of Appeal was correct.

40 With these comments in mind Chitty says that:[80]

> The exclusion of liability for 'consequential loss or damage' will not cover loss which directly and naturally results in the ordinary course of events from the breach, but only loss which is less direct or more remote … some of these cases may be decided differently today …

41 It is not clear that courts are so willing. In, for example, *Ease Faith v Leonis Marine Management*[81] in 2006 the court persisted with the notion that 'consequential' meant not direct, that loss of profit might be direct or indirect, and that the loss of profit claimed was direct, although Andrew Smith J declined to describe a lower than agreed sale price as loss of profit: 'the loss … is more akin to a diminution of price than a loss of profit'. The higher a price, the higher a profit, *ceteris paribus*, and vice versa.

42 The next case, in 2008, in which the issue was considered, *Ferryways NV v Associated British Ports*,[82] is a more difficult one, the death of a serving officer being involved, in which Ferryways's Chief Officer was killed by the negligence of an employee of the defendant stevedores' subcontractor. Ferryways claimed the death benefit and the repatriation expenses, which Teare J found to be 'a loss which flows directly and naturally from the Defendant's breach of duty' (limb one) and defeated an exemption clause which excluded the stevedores' liability for indirect or consequential loss 'including without limitation … the liabilities of the Customer to any other party'. This seems to be a commercially reasonable result.

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77 Daintith and Willoughby, above, n 11.

78 *Caledonian North Sea Ltd v British Telecommunications Plc* [2002] 1 All ER (Comm) 321; [2002] UKHL 4 at [8].

79 *Caledonian North Sea Ltd v British Telecommunications Plc* [2002] 1 All ER (Comm) 321; [2002] UKHL 4 at [100].

80 *Chitty on Contracts*, above, n 23 at 17-009.

81 *Ease Faith Ltd v Leonis Marine Management Ltd* [2006] 2 All ER (Comm) 422; [2006] EWHC 232 (Comm) see esp [145].

82 *Ferryways NV v Associated British Ports* [2008] 1 Lloyd's Rep 639; [2008] EWHC 225 (Comm).

An opportunity to act on the House of Lords' views then appeared in 2009 in *GB Gas Holdings Limited v Accenture (UK) Ltd (Accenture)*[83] when GB Gas pursued Accenture for upwards of £183,000,000 in respect of alleged defects in a new IT system (the 'Jupiter System') supplied by Accenture. The contract included a clause which ran as follows: 43

> 16.2 Consequential Loss
>
> … in no event shall either Party be liable whether in contract, tort (including negligence) or otherwise in respect of any of the following losses or damages:
>
> 16.2.1 loss of profits or of contracts arising directly or indirectly;
>
> 16.2.2 loss of business or of revenues arising directly or indirectly;
>
> 16.2.3 any losses, damages, costs or expenses whatsoever to the extent that these are indirect or consequential or punitive; …

The courts reviewed claims which included sums of £18.7 million for distribution charges, £8 million in ex-gratia compensation paid to customers to reflect billing difficulties and poor customer service, £2 million in additional borrowing charges due to the late billing or non-billing of customers, and other sums incurred in chasing debts, additional stationery and correspondence costs and reached the conclusion that these sums were a direct result of errors in the system, the Court of Appeal overturning the High Court on the ex-gratia payments.[84] This produced the very odd effect that loss of revenue (profit), a likely direct and limb one loss, was excluded in terms whereas clearly limb two costs such as additional borrowing charges and a more than somewhat remote 'loss' of voluntary ex-gratia payments were held to be direct and limb one. It is highly unlikely that this is what the parties intended.[85] 44

In 2011, Mr Recorder Acton Davis QC construed a contract for a system intended to remove hydrogen sulphide from biogas produced in the claimant's waste water treatment processes at its Whittlesey plant, in which the parties had agreed that 'in no event however will Seller be responsible for indirect, special, incidental and consequential damages'. He found, citing *Croudace,* that losses, including additional utility costs, employee time, lost revenue for Renewable Obligation Certificates (which seems on its face to be a limb two candidate) were direct. [86] The oddity that contemporaneous records of employee time were not required is repeated in this case, the 45

83 [2009] EWHC 2734 (Comm).

84 In the US similar losses were held to be consequential in *Heartland Payment Sys, Inc Customer Data Sec Breach Litig,* 834 F Supp 2d 566 at 580 (SD Tex 2011).

85 See Michael Bywell and Scott Cummins, 'Exclusions of Consequential Loss: an Australian Perspective' *Society for Computers and Law* 2013 for a comparison of the likely Australian (Peerless) outcome with the English outcome.

86 *McCain Foods GB Ltdv Eco-Tec (Europe) Ltd* [2011] EWHC 66 (TCC) at [63] and [80].

judge saying, eccentrically, that 'There is no material before me upon which I can conclude that the sum claimed is unreasonable'.[87]

46 In 2013 in *Elvanite Full Circle Ltd v AMEC Earth and Environmental (UK) Ltd*[88] Coulson J denied a claim for loss of profit on the basis that the profit claimed was indirect, referring back to Sedley J's comment in *Hilton* above that loss of profit to the hotel itself, as opposed to profits from the minibars, might be 'consequential'.

47 In 2014 another small crack appears in the dam. Moore-Bick LJ, conceding that 'the expression "consequential loss" has caused a certain amount of difficulty for English lawyers'[89] (including judges!) found that 'spread costs', being additional overheads[90] claimed in a case in which many losses were excluded in the following terms:

> i) any indirect or consequential loss or damages under English law and
>
> ii) loss or deferment of production, loss of product, loss of use … loss of business and business interruption, loss of revenue

48 were, in context, consequential, and that the purpose of **ii** was 'clearly to catch consequential losses of all kinds'.[91] The decision, despite casting doubt on *Saint Line*, *Croudace* and *Deepak,* is predicated on the correct construction of the contract, and sidesteps any question as to whether the losses are limb one or limb two of *Hadley v Baxendale*.[92] Also in that year, however, the *Croudace* view (indirect = limb two/direct = limb one) was cited with apparent approval in a case where Cooke J managed to partly avoid the issue by declining to accept that a contract price/market price differential was a loss of profits claim.[93]

49 In 2016 there is another small dent in the dam in *Star Polaris,* in which Sir Jeremy Cooke upheld an arbitral decision regarding a contract which excluded liability for 'consequential or special losses, damages or expenses', in the context of an apparent attempt by the buyer to sidestep an exclusive warranty. The arbitrators considered 'consequential', when read together with the exclusive warranty, '… to mean that which follows as a result or consequence of physical damage, namely additional financial loss other than the cost of repair or replacement', the OED's first meaning. Sir Jeremy Cooke ruled that 'What Article IX.4(a) does is to make it plain that there is no

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87 [2011] EWHC 66 (TCC) at [86] and see *Tate & Lyle Food and Distribution Ltd v Greater London Council* [1981] 3 All ER 716. McGregor, above, n 16, para 31-018 refers to such damages as consequential, citing a Scots case in which the need for evidence was stressed: *Johnston v W H Brown Construction (Dundee) Ltd* [2000] BLR 243; 2000 SLT 791.

88 *Elvanite Full Circle Ltd v AMEC Earth & Environmental (UK) Ltd* [2013] EWHC 1191 (TCC).

89 *Transocean Drilling UK Limited v Providence Resources Plc the Arctic III* [2014] EWHC 4260 at [15] (Comm) (*Transocean*).

90 *Transocean* [2014] EWHC 4260 at [3].

91 *Transocean* [2014] EWHC 4260 at [25].

92 *Transocean* [2014] EWHC 4260 at [15].

93 *Glencore Energy UK Ltd v Cirrus Oil Services Ltd* [2014] EWHC 87 (Comm) at [96] and [98] 'The contract price/market price differential is not a computation of lost profit'.

liability above and beyond the express obligations undertaken by the Yard and, in particular, without prejudice to that, financial losses consequent upon physical damage are not covered by the guarantee'.[94] Older decisions pointing to a 'well-recognised meaning',[95] were distinguished rather than overruled.

50 And, in the next opportunity for a thorough review O'Farrell J, in *Entertain Video Ltd v Sony DADC Europe Ltd*,[96] in 2020 rejected alignment with *Transocean*. A group of young men had attacked Sony's warehouse during rioting after the shooting by police of Mark Duggan. Under a logistics contract Sony stored and distributed Entertain's material, who claimed damages for lost profit and business interruption. The contract included the following exclusion clause:

> 10.3 Neither party shall be liable under this Agreement … 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.

51 Following a review of the *Croudace* line of authority, citing many of the above cases, O'Farrell J ruled that 'there is no definition of indirect or consequential loss in the Logistics Contract that would indicate a wider meaning than the second limb of *Hadley v Baxendale*' inferring that indirect and/or consequential means limb two.[97]

52 In 2021 in Northern Ireland, faced with an exclusion of '"… any indirect special or consequential loss or damage…."' Sir Ronald Weatherup persisted with the view that this meant that the term 'excludes liability for indirect, special or consequential loss or damage but does not exclude liability for direct loss and damage' and found that damages, including for a reduction in selling prices and revenue (neither being lost profit!), were direct, while agreeing that some minor 'extra credits' were indirect. These credits seem to be unconnected with the defects and so irrecoverable in any event as the judge observed that they were 'a discount made to secure a further order rather than being a direct result of the defects'. [98]

53 More recently, in 2022, the Court of Appeal found wasted expenditure to be of a different category of loss to loss of profit in a case where loss of profit was clearly excluded but Coulson LJ again muddied the water saying (my italics) that 'The types of loss expressly identified by the particular words of clause 23.3 at the heart of this case (loss of profit, revenue, savings) are all of a similar kind. They are *often* considered to be types of consequential

94 *Star Polaris* [2017] 1 Lloyd's Rep 203; [2016] EWHC 2941 (Comm) esp at [38]–[39].

95 *Ferryways NV v Associated British Ports* [2008] 1 Lloyd's Rep 639; [2008] EWHC 225 (Comm) at [82]–[84].

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

97 *Entertain Video Ltd v Sony DADC Europe Ltd* at [239].

98 *BA Kitchen Components Ltd v Jowat (UK) Ltd* [2021] NIQB 3 at [33] and [55]–[62].

loss',[99] also observing that wasted expenditure is not usually considered to be consequential loss.[100]

54 The term 'consequential' might randomly help in the US; West's very good survey of the case law, noting that 'American courts do not appear to follow a bright-line rule that certain types of losses are always consequential and certain other types of losses are always direct or general', impelling him to quote Michael Polkinghorne of the firm White and Case saying that:[101]

> The first problem with the term 'indirect and consequential loss' is a fundamental one: no one agrees on what it means. Not even between common law jurisdictions, not even within common law jurisdiction.

55 We can see that the courts seldom attempt to ascertain 'what a reasonable person … would have understood the parties to have meant'[102] once the word 'consequential' appears. Indeed, challenged on the point, they can become quite difficult, Waller LJ ticking commercial players and drafters off:[103]

> … once a phrase has been authoritatively construed by a court in a very similar context to that which exists in the case in point, it seems to me that a reasonable businessman must more naturally be taken to be having the intention that the phrase should bear the same meaning as construed in the case in point.

56 This is not objective; it can best be compared with Humpty Dumpty's method of construction as expounded in the immortal words of Lord Atkin (disagreeing with Lord Maugham in this case):[104]

> I know of only one authority which might justify the suggested method of construction. 'When I use a word', Humpty Dumpty said in rather a scornful tone, 'it means just what I choose it to mean, neither more nor less'. 'The question is', said Alice, 'whether you can make words mean different things'. 'The question is', said Humpty Dumpty, 'which is to be master — that's all'…

57 Waller LJ's approach is subjective and dogmatic. It is more likely that Lord Wright's understanding is that of the reasonable businessperson. As Carter[105] says, the prevailing *Croudace* view means that a bare exclusion of 'consequential' loss will 'generally have no impact on … claim for damages' and it is hard to believe or argue that rational commercial parties intend to include a wholly pointless term. The detail of cases above shows that, despite *Investors,* despite Chitty and other eminent textbook authors or

99 *Soteria Insurance Ltd v IBM Ltd* [2022] EWCA Civ 440 at [66].

100 *Soteria Insurance Ltd v IBM Ltd* [2022] EWCA Civ 440 at [69].

101 West, above, n 3 at 990–1 and at n 111.

102 *Chitty on Contracts,* above, n 23 at 15-054 — 'The court is concerned … to ascertain what a reasonable person … would have understood the parties to have meant'.

103 *British Sugar* (1997) 87 BLR 42.

104 *Liversidge v Anderson* [1942] AC 207 (*Alice Through the Looking Glass*, c vi), also cited by Lord Hoffmann in *Investors* as a riposte to Leggatt LJ.

105 Carter, above, n 2 at 126.

editors, despite the House of Lords' and the Supreme Court's doubts as to the validity of the approach, the High Court sticks, limpet-like, to the tired old hull of precedent, Sir David Foxton arguing that 'If any of the old "intellectual baggage" of the construction of exemption clauses is to be jettisoned, this looks a prime candidate'.[106] Although there are some signs that the courts will now differentiate between 'indirect' and 'consequential' it thus appears to have a merely marginal effects on minor claims.

The Real-world and Consequential Loss

In many commercial enterprises, contracts or legal departments will offer management, sales, engineering, project management and procurement colleagues training on contract topics and 'consequential loss' is almost certain to be addressed. An open question to engage one's audience is useful. For example, and I write from experience, the question 'What does consequential loss mean' often elicits something akin to Nettle JA's analysis in *Environmental Systems*:[107] 58

> … everything beyond the normal measure of damages, such as profits lost or expenses incurred through breach.

These limitation clauses are the hardest fought in commercial negotiations, both as matters of principle and in the detail of the drafting, as many annual reports from World Commerce and Contracting's member survey show (there are 70,000 members).[108] 59

Top ten most negotiated terms 2018

'18			'15	'14/'13	'12	'11	'10	'09	'08	'07
1	Limitation of Liability	–	1	1	1	1	1	1	1	1
2	Indemnification	–	2	3	2	2	2	2	2	2
3	Price/Charge/Price Changes	–	3	2	3	3	3	3	3	4

Inspired by a recent US attorney's experience,[109] I asked ChatGPT 'what is consequential loss in contract?' and received this answer, reasonably accurate as a matter of commercial vernacular but 100 per cent wrong as a matter of law: 60

> Consequential loss in contract refers to the indirect and secondary loss or damage arising as a result of a breach of contract. It refers to losses that go

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106 David Foxton, 'The Status of the Special Rules of Construction of Exemption Clauses in Commercial Contracts' (2021) *JBL* 205 at 214.

107 *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* (2008) 19 VR 358; [2008] VSCA 26 at [93].

108 For example, World Commerce and Contracting, *Most Negotiated Terms 2022 — Negotiating in a Time of Turmoil* (2023), IACCM, *2013/2014 Top Terms*' (2014).

109 A lawyer used ChatGPT to prepare a court filing. It went horribly awry — CBS News — 'In this case, the AI invented court cases that didn't exist, and asserted that they were real'.

beyond the immediate loss or damage caused by the breach of contract and includes loss of profits, loss of use, loss of business opportunities or reputation, and other damages that may result from the breach of contract.

61 World Commerce and Contracting ran a similar, more scientific exercise in 2018 and reached a similar conclusion, their consultant Daphne Perry recording that 'This survey is now one more reason for a court to give a more natural meaning to indirect and consequential loss, as some American, Australian and Scottish courts have done'.[110]

62 The commercial or contract expert is likely to take calls from anxious executives or engineers who need to ascertain likely liability when, say, a baggage handling line stops, a gas turbine has suffered a 'haircut', a mine-winder has developed a judder, a ship's car-lift needed to offload cars in New York has broken down or an emergency offshore evacuation system has failed on test. These executives need commercial advice on the scale of the problem and to make sure that commercial colleagues are in a position to determine commercial next steps. They also want reassurance on liabilities; they may well be measured on, or have incentives based on, contract financial performance. The best initial advice is usually to make sure they take things safely, but to identify the problem and get things up and running as soon as possible.[111] Deal with the money later. The primary concern should always be safety, then production and as a close third consequential loss liability. These front-line managers or technicians do not enquire about liability for financial and economic loss, whether direct or indirect, whether special or foreseeable and so on but refer only to 'consequential loss' or 'consequentials'. The expert in charge of the process will also often take calls from team members desperate for advice on the wording of a 'consequential loss clause'.[112]

63 Chitty says that courts assume that the parties 'have used language in the way that reasonable persons ordinarily do' and that terms are '… to be understood in their plain, ordinary, and popular sense', [113] with the aim of ascertaining 'what a reasonable person … would have understood the

110 Daphne Perry, *What is Indirect and Consequential Loss?,* World Commerce and Contracting, 2018. See also Wifa Eddy Lenusira, 'Conflicts and Uncertainties in English and Scottish Judicial Interpretation of Consequential Loss and its Application to the United Kingdom's Oil and Gas Industry' (2015) 56 *International Energy Law Review* 56.

111 This advice was given to me very early in my career by one of GEC's most senior lawyers who told me that judges disapprove of companies who cavil about defect liability issues.

112 My advice/instruction to my team once read: 'You should until further notice refer consequential loss clauses to me in particular where, there is no "paramount" language in the consequential loss exclusion, general words precede the specific words, the list of specific words does not clearly cover baseline requirements … loss of profit, loss of production, any linkage between the general & the specific is implied or expressed; such as "including" or "any other", where loss in all legal theory is not clearly excluded …, where there is no "catch all" of financial or economic loss, where the general list is too limited'.

113 *Chitty on Contracts,* above, n 23, para 15-063 citing *Robertson v French* (1803) 4 East 130; 102 ER 779.

parties to have meant'.[114] The 'proper meaning',[115] the popular sense of 'consequential', its 'natural meaning'[116] variable in context, as we have seen from multiple Lords of Appeal, professional and student textbook authors, and from commercial players, is financial or economic loss, usually wholly or partly uninsurable (particularly in equipment supply or construction contracts), and uncontrollable by the breaching party, consequent on a breach of contract. This is what commercial players mean when they use the term, an argument strengthened by the divisor in insurance contracts. In an early edition of Hudson, for example, Ian Duncan-Wallace QC, not being noted for careless use of language, includes in a list of consequential losses, 'loss of profit, loss of overhead recovery … and disturbance'.[117] And Anthony Ogus was of the same opinion, defining consequential loss (in tort) as including 'compensation for being deprived … of profits and earnings …'.[118] As Carter argues, 'as a commercial concept, 'consequential loss' is no more concerned with measure of damage (the McGregor view) than remoteness of loss (the *Croudace* view)'; it is, in fact, I argue, concerned with type or genus of loss.

A Modest Proposal

Pressed for a definition of consequential loss in the air in a bare exclusion clause or where it is coupled with indirect or linked to a laundry list (consequential loss including loss of profit …), I suggest that the commercial meaning aligns, in principle, somewhat with the insurance contract meaning. The intention in insurance is to insure primarily physical loss but exclude other losses. Physical loss cannot readily be extended in meaning to include the cost of installation or removal, together with costs incurred by the buyer in the course of repair or replacement. But the analogy is that consequential loss means those costs and losses which are metaphysical *and* which go beyond the costs and losses involved with a rejection and/or a replacement and the associated costs of running a sub-optimal system or machine in the interim. This aligns with the classical or typical clause we see in the MF/1 form; discussed further below. It also aligns a little with Coulson J's comment in *Elvanite* that, reviewing a loss of profit claim, although, as noted above, the *Hadley v Baxendale* divisor does not 64

114 *Chitty on Contracts,* above, n 23, para 15-054.

115 A reference to *McGregor on Damages*, 17th ed, Sweet & Maxwell, London, 2003, paras 1-037–1-039.

116 Possibly the lost meaning lamented by Sedley LJ in *Hotel Services* [2000] BLR 235; [2000] EWCA Civ 74 at [11].

117 Hudson and Wallace, above, n 11, pp 597–8. Keating, above, n 52, para 20-068 also says 'Consequential loss, i.e., loss of profit …'. The latest edition of Hudson, above, n 9, refers to wasted expenditure, loss of use and distress and inconvenience as consequential at 7-030. Interestingly, perhaps, the 1994 27th edition of *Chitty* agrees with the *McGregor* and *Benjamin* descriptions of limb two loss and damages in addition to the claim for the price as consequential — see para 41-273.

118 A I Ogus, *The Law of Damages,* Butterworths, London, 1973, p 18.

work when type of loss is in question, determining whether the loss was consequential or not:[119]

> Traditionally, the cost of putting right the thing itself, such as the cost of remedial works or the cost of replacement, was thought to fall within the first limb, whilst claims which arise out of the contracting parties' knowledge that any breach would have particular consequences … came under the second limb. A claim for loss of profit would usually fall into this category.

65 In trying to create a dividing line beyond which losses might be subject to a default definition that they are consequential it is worth thinking about a few cases. The older cases, *Millar's, Saint Line* and *Hotel Services* involve machinery or equipment which does not work and is rejected. In more recent cases IT is involved and, likewise, systems are rejected.

66 As I discuss above the decision in *Millar's* in which the costs of a new machine and the associated costs of dismantling the rejected machine were classed as not consequential seems to be commercially sound. Expanding the point to the modern day and considering *Pegler v Wang* and *Accenture* those costs involved in uninstalling a rejected IT system, configuring a new system and the in-between administration and resurrection of legacy systems also seem to be the sort of costs that would not generally thought of as consequential. Sir Jeremy Cooke grasped this point when agreeing with the decision of the Arbitrators in *Star Polaris,* when the Arbitrators had also determined that, in the context of the case and the contract drafting, consequential loss was a type/genus of loss, ruling that:[120]

> '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.

67 So, in the case of, say, a steam turbine that failed on test, a buyer would have to dismantle it, dig out or alter its foundations and put in new foundations. Those costs seem to me to be defect rectification costs and the supplier's core liability. More difficult is the cost of, say, imported steam or energy which might cost more during the period between the removal of the rejected machine and the commissioning of its replacement. In *Accenture* the additional stationery costs and those of writing to customers might be rectification costs as opposed to consequential loss. Likewise in *Pegler v Wang* claims for substitute software and consultancy services as well as microfiching might be regarded as rectification costs.

68 West, discussing M&A deals, advises the use of clauses which avoid 'the use of … terms that could potentially affect the basic market measure of

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119 *Elvanite Full Circle Ltd v AMEC Earth & Environmental (UK) Ltd* [2013] EWHC 1191 (TCC) at [304].

120 *Star Polaris* [2017] 1 Lloyd's Rep 203; [2016] EWHC 2941 (Comm) at [39]. Notably at [40] he said that diminution in value would be a first limb loss but held that it was excluded under the terms of the contract.

damages for direct claims'.[121] My objective, in the type of deals I discuss, is similar, being the protection of the basic asset value promised to the purchaser, but placing the enterprise risk where it belongs: with the purchaser.

Despite the advice of West and Duran who say that the word 'consequential' should 'be stricken from the deal lexicon',[122] and always aware of the potential exasperation of colleagues when pedantic drafting issues took ages to resolve it was still worthwhile explaining, internally and to negotiators, why best practice was to agree something like the MF/1 clause (with an appropriate laundry list in, for example, baggage handling covering off payments to passengers for late bag arrivals):[123] 69

> Neither the contractor nor the purchaser shall be liable to the other by way of indemnity or by reason of any breach of the contract or of statutory duty, (including but not limited to negligence) for any *loss of profit, loss of use, loss of production, loss of contracts* or for any financial or economic loss or for any indirect or consequential damage whatsoever that may be suffered by the other.

From the drafting one can see that, for example, costs of replacement of defective equipment, defect rectification and the like are not 'consequential' but loss of profit, loss of use and the like are 'consequential'. One can also see that the drafting, separating the laundry list, then setting out an omnibus exclusion of financial and economic loss and then keeping indirect and consequential as a stand-alone category avoids the problem that trapped, for example, Wang in *Pegler v Wang*.[124] A clause following these strictures successfully excluded liability for lost profit and wasted employee time: 70

> neither the Contractor or the Owner shall be liable one to the other for any loss or deferment of anticipated or actual profit, loss of revenue, loss of use, loss of production, loss of efficiency, or operating materials, business interruption or similar damage or for consequential or indirect losses arising from or arising out of or in connection with the Project or the performance thereof or any act or omission relating thereto howsoever caused whether in contract, tort or otherwise at law.[125]

121 West, above, n 3 at 1001–2.

122 Glenn D West and Sara G Duran, 'Reassessing the "Consequences" of Consequential Damage Waivers in Acquisition Agreements' (2008) 63 *Bus Law* 777 at 807.

123 See, eg *London Fire and Emergency Planning Authority v Halcrow Gilbert Associates Ltd* [2007] EWHC 2546 (TCC); (2008) 24 Con LJ 103. For a case in which a laundry list did not work, and there was no catch-all see *Accenture (UK) Ltd* [2009] EWHC 2734 (Comm).

124 See also *Ferryways NV v Associated British Ports* [2008] 1 Lloyd's Rep 639; [2008] EWHC 225 (Comm).

125 *Decoma UK Ltd v Haden Drysys International Ltd* Ltd [2005] EWHC 2948 (TCC) at [102] and [167]. Note the expanded laundry list.

71 By 2009, in an oil and gas environment, taking the case law into account meant that the wording of clauses evolved to:[126]

> Neither party shall be liable to the other by way of indemnity, breach of contract or of statute, tort (including negligence in whatever form) or any other legal theory for any loss of profit, loss of use, loss of production (including loss of hydrocarbons), loss of contracts, loss of revenue or of anticipated savings, any increase in operating costs, loss of information and data or for any financial or economic loss or for any indirect or consequential damage whatsoever that may be suffered by the other.

72 Another possible method is that used in *Star Polaris*, which involved providing remedies for defect rectification and excluding all other liability. The drafting there provided, in part:[127]

> 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.

73 This operated to exclude liability for all financial losses caused by breach of contract, save for the cost of replacement and repair. However, better practice entails a laundry list in MF/1 style and a catch-all in MF/1 style.[128] Perhaps this is belt and braces advice but when liabilities can reach multiples of the contract price and judges are so hostile to exclusion clauses an abundance of caution is justified.

74 It is worth explaining why I persevere with the word 'consequential' despite a seeming lack of real legal meaning in it from precedent. One reason is that the MF/1 and similar drafting, which includes the word, is effective, Toulmin J describing it as 'intended to specify categories of loss which are to be excluded',[129] although a visit to the London library of the Institution of Mechanical Engineers for a review of the historic development of their standard forms showed that 'consequential' as a term only made an appearance in 1976, the earlier Model Forms (A) preferring a simpler

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126 See eg Lucy Garrett, 'Consequential Loss Exclusion Clauses: the Pitfalls' (2014) in *Construction Law Blog* in Practical Law advising that 'The key when drafting is carefully to consider precisely what losses are likely to flow from a breach of contract, and then specifically to identify those types of losses in the exclusion clause'.

127 *Star Polaris* [2017] 1 Lloyd's Rep 203; [2016] EWHC 2941 (Comm) at [9].

128 Above, n 67.

129 See *London Fire and Emergency Planning Authority v Halcrow Gilbert Associates Ltd* [2007] EWHC 2546 (TCC); (2008) 24 Con LJ 103 at [412]. See also the Institution of Chemical Engineers' Red Book of 2007: 'Neither the Contractor nor the Purchaser shall be liable to the other for … (b) loss or deferment of actual or anticipated profit, loss of revenue, loss of use, loss of production, business interruption, or any similar damage or for any consequential or indirect losses of any kind …'.

exclusion of loss of use, loss of profit or loss of contracts.[130] Another is that it might just act as a long stop; as in *BA Kitchen Components*. The third is that one should worry about providing an imaginative judge with a loophole from which to assume that because consequential loss is not expressly covered it is therefore recoverable.

Even in the event of a Supreme Court decision which applied 75
something like the meaning or logic used by Nettle J, and made it clear that ‘consequential’ in contract usually connotes a type of loss, it still seems appropriate to persist with the certainty of an exclusion of consequential loss, and not be tempted to gamble that context will prevail, given the malleability of the word ‘consequential’, noting, for example, the US case law cited by West, that the rule in *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* has been described as particular to that case and not a general rule even in Australia,[131] and that the courts have missed many opportunities to take heed of previous senior judicial hints and comments.

130 I acknowledge the generous assistance of Sarah Rodgers who found me the right boxes of forms going back to 1928 and the generosity of the I Mech E in permitting me the use of their splendid library.

131 See *Patersons Securities Ltd v Financial Ombudsman Service Ltd* (2015) 108 ACSR 483 and *Regional Power Corp v Pacific Hydro Group Two Pty Ltd* (2013) 46 WAR 281; [2013] WASC 356. The *Peerless* rule was upheld in *Alstom Ltd v Yokogawa Australia Pty Ltd (No 7)* [2012] SASC 49. For a review of the issue in financial mis-selling see Peter Dodge, ‘Consequential Loss Exclusions in Financial Misselling Claims’ (2017) 5 JIBFL 277.