

Webinar:

“Use of Consequential Loss Exclusion Clauses”

Mino Han – Peter & Kim

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WEBINAR

BARTON
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USE OF CONSEQUENTIAL LOSS IN EXCLUSION CLAUSES

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24 February 2022

Let me share a story with you: Back in 2015...

CASE

A. Facts

The Contract

- » An EPC main contractor (“MC”) for a power plant and sub-contractor (“SC”) entered into a supply contract. Under this subcontract, the SC was responsible for the manufacture and supply of a main equipment (turbine, generator) for a power plant.
- » Governing law of this supply contract was Korean law.
- » The supply contract has a typical exclusion clause under which the parties are excluded from liability arising from indirect or consequential loss.

CASE

A. Facts

Breach of contract

- » SC supplied the main equipment to MC within the agreed period under the supply contract.
- » A few months later, a major defect in the main equipment was found.
- » The main equipment had to be replaced.
- » However, due to the replacement, the commissioning works were significantly delayed.

CASE

A. Facts

Consequences of the breach

- » Under the main contract, due to the delay in completion, the MC had to pay Liquidated Damages (“LD”) to the employer (“E”) in the amount of USD 400k.
- » Apart from the defective main equipment, MC was ready for completion of the works. In MC’s view, the delays were solely due to SC’s fault.

CASE

A. Facts

Dispute between the parties

- » MC sought to recover these LDs (under the main contract) from SC as general damages.
- » SC said that the USD 400k did accrue under a contract different from the supply contract, that the amount was hence a ‘consequential loss’ at best and therefore falls under the exclusion clause.

CASE

B. Today's topics

- » Interpretation of an Exclusion Clause?
- » Meaning of 'Consequential Loss' in an Exclusion Clause?
- » Threshold between Limb 1 and Limb 2 in Hadley v Baxendale?

CASE

C. Governing Law

- » What if the governing law of the supply contract was English law (and not Korean law)?
- » King's College London dissertation (2018)
 - “The Meaning and Scope of ‘Consequential Loss’ in Exclusion Clauses - A comparative law analysis between English law and Korean law”

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I. EXCLUSION CLAUSE

II. MEANING OF “CONSEQUENTIAL LOSS”

III. LIMB 1 v LIMB 2

IV. CASE ANALYSIS

I. EXCLUSION CLAUSE

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- **How does a typical exclusion clause look like?**

- » **FIDIC Red Book 1999 Sub-Clause 17.6 (or 2017 ed. Sub-Clause 1.15):**

“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]”

I. *EXCLUSION CLAUSE*

■ **Validity**

- » Deemed valid, unless subject to statutory control
- » Unfair Contract Terms Act 1977 (UCTA)
 - Article 3
 - Written standard terms
 - Reasonableness

I. EXCLUSION CLAUSE

■ Validity

- » UCTA – how powerful is this?
- » *Saint Gobain Building Distribution v Hillmead Joinery* [2015]
- » What about Korean Law? => Korean Act on the Regulation of Terms and Conditions

I. EXCLUSION CLAUSE

▪ Interpretation

- » Is there anything special?
- » Traditional Approach: narrow interpretation (*Canada Steamship v R* [1952])
- » Recent Trend: The court refrains from any special methods of construction (*Photo Production Ltd v Securicor Transport Ltd* [1980])
- » Korean Law? Principle of 'Strict Interpretation' (93Da3103):
 - “[i]f any term of a contract relied on by either party thereto imposes material liability on the other party, the text of such term should be more strictly interpreted.”

II. MEANING OF “CONSEQUENTIAL LOSS”

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- **General Principle on Damages**

- » *Hadley v Baxendale* [1854]

- Limb 1: Damages arising naturally (i.e., according to the usual course of things) from the breach of contract itself
- Limb 2: Damages that may be reasonably supposed to have been in the contemplation of both parties at the time they made the contract.

- » According to Korean Law? Ordinary damages v special damages

II. MEANING OF “CONSEQUENTIAL LOSS”

▪ Meaning of “Consequential Loss” in Indemnification Clauses

» “Consequential loss” = Any losses that are consequential?

» “Consequential loss” = Limb 2

(*Croudace v Cawoods* [1978], *BHP Petroleum v British Steel* [2000],
Hotel Services Ltd v Hilton International Hotels [2000], *Ferryways NV v Associated British Ports*
[2008])

» **Exception:** *Star Polaris LLC v HHIC-Phil Inc* [2016]: “decisions concerning particular contracts (or clauses) do not create binding precedent (stare decisis) in relation to other contracts on different terms”

II. MEANING OF “CONSEQUENTIAL LOSS”

- **Meaning of “Consequential Loss” in Indemnification Clauses**

- » *2 Entertain Video Ltd & Ors v Sony DADC Europe Ltd* [2020]

“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.”

- » According to Korean Law?

III. LIMB 1 v LIMB 2 - Where to draw the line?

III. LIMB 1 v LIMB 2

- **No English court precedent concretely setting out where to draw the line between limb 1 and limb 2 losses.**

III. LIMB 1 v LIMB 2

▪ **Analysis of court cases**

- » Would the loss have arisen naturally ‘in the great multitude of cases’ as a result of a breach of contract?
- » Would a reasonable businessman in the parties’ shoes, who understands the ordinary practices and exigencies of the other's trade or business, have realized that such loss was sufficiently likely to result from the breach of contract?
- » Was there a ‘real danger’ or ‘serious possibility’ that the kind of loss would have occurred as a result of the breach of contract?
- » Has the loss arisen from the breach without any other intervening cause and independently of special circumstances?

III. LIMB 1 v LIMB 2

- **Analysis of court cases – what was considered when distinguishing Limb 1 and 2?**
 - » Significance of the goods (*Croudace v Cawoods*)
 - » Availability of the goods (*Portman v Middleton and another*)
 - » Occupation of the supplier / sub-contractor and commercial relationship with the purchaser (*Croudace v Cawoods*; *Fyffes Group v Reefer Express Lines*)
 - » Likelihood of third-party contract (*Croudace v Cawoods*, *Sylvia Shipping v Progress Bulk Carriers*)
 - » Likelihood of third-party claim (*Ferryways NV v Associated British Ports*; *Siemens Building Technologies FE Ltd v Supershield Ltd*; *Sylvia Shipping v Progress Bulk Carriers*)
 - » Relationship between contracts (*Portman v Middleton and another*)

III. LIMB 1 v LIMB 2

- **Distinguishing ordinary damages and special damages - Korean court?**
 - » Relationship between supplier / sub-contractor's breach of contract and third-party's damages (2005Da55312)
 - » Occupation of the supplier / sub-contractor and commercial relationship with the purchaser (2004Gahap9444, 91Da25369)
 - » Social circumstances (2004Gahap9444)
 - » Status of the third-party (2014Na8393)

IV. CASE ANALYSIS

IV. CASE ANALYSIS

- **Governing law of supply contract: English Law**
 - » Significance of the goods: main equipment
 - » Availability of the goods: bespoke
 - » Occupation of the supplier / sub-contractor and commercial relationship with the purchaser: supplier was manufacturing main equipment and knew well about the construction process
 - » Likelihood of third-party contract: main contract
 - » Likelihood of third-party claim: LD clause in the main contract
 - » Relationship between contracts
 - » Intervening cause or act by the contractor?

IV. CASE ANALYSIS

- **Governing law of supply contract: English Law**
 - » Quantum?
 - » *Victoria Laundry v Newman Industries* [1949]
 - Claimant's losses suffered under "contracts to be reasonably expected": recoverable
 - Additional losses suffered under unexpected "particularly lucrative dyeing contracts": not recoverable
 - What does that mean?

IV. CASE ANALYSIS

- **Governing law of supply contract: Korean Law**
 - » Similar outcome
 - » Principle of ‘Strict Interpretation’
 - » Korean Act on the Regulation of Terms and Conditions
 - » Fewer court cases for reference
 - » No case law or jurisprudence distinguishing quantum found

V. PRACTICAL SUGGESTIONS

V. PRACTICAL SUGGESTIONS

- **Suggestions**

- » Use contractual terms in an exclusion clause that are **known and used** in that jurisdiction
- » Specifically **define** the meaning of ‘consequential loss’ in the contract in order to remove ambiguities and thereby reduce any subsequent risks.

Thank you!

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QUESTIONS



NEXT WEBINAR

31 March 2022 | 11:00 AM GMT

African Procurement – The Way Forward

Dr Tett Walters, FIDIC Consultant (Ghana)

FIDIC

Karen Gough, 39 Essex Chambers (UK)

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Thank You



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