Exclusion of Liability, Limitation of Liability and Consequential Loss: 
*Regional Power Corporation Rejects the Peerless Formulation*

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Author/s: Kieren Parker

**Executive summary**

It is common for parties who enter into a contact to agree that, if one party breaches the contract, its liability to the other will be limited in certain ways. A question that Australian courts have been grappling with for the past six years is where to draw the line in calculating damages when the contract expressly excludes 'consequential loss'.

Recent Supreme Court cases starting with *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* have departed from the English authorities on the construction of 'consequential loss' clauses. In *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd [No 2]*, the Supreme Court of Western Australia casts doubt on the Peerless decision, but adds no more clarity to the interpretation of 'consequential loss'.

A limitation of liability clause that excludes simply "consequential loss" will leave a lot to chance. *Regional Power* only reinforces that contracting parties should clearly state the scope of damages to be excluded as consequential loss.

**Peerless recap - the new formulation**

In *Peerless*, Nettle JA held that the true distinction is between:

- normal loss, which is loss that every plaintiff in a like situation will suffer; and
- consequential losses, which are anything beyond the normal measure, such as profits lost or expenses incurred through breach.

Applying *Darlington Futures Ltd v Delco Australia Pty Ltd* to the decision in *Peerless* sought to restore the term 'consequential loss' to its "ordinary and natural meaning".

**Regional Power - rejection of any formulation**

The plaintiff in *Regional Power*, a statutory authority with responsibilities to deliver electricity to remote communities in WA, claimed damages under a power purchase agreement with the defendant by reason of the defendant's failure to deliver energy to the plaintiff following an outage at the defendant's power station. The agreement contained an exclusion clause which meant that the defendant was not liable to the plaintiff "for any indirect, consequential, incidental, punitive or exemplary damages or loss of profits.”

The Court found it unhelpful to assess the meaning of consequential (or indirect) loss or damage "by some fettering predisposition" towards either loss falling under the second limb of the rule in *Hadley v Baxendale*, or the replacement construction proposed in *Peerless*. In Martin J's view, *Darlington v Delco* meant that any such predisposition is to be rejected.

**Taking stock: the position following Regional Power**

Following *Regional Power*, the position is that an exclusion of consequential loss clause is determined according to *Darlington v Delco*, 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 appropriate, construing the clause contra proferentem [against the party who holds the benefit of the clause] in case of ambiguity."

The problem is that the term 'consequential loss' has a subjective, rather than a natural and ordinary, meaning. This is borne out by the recent decisions. In *Alstom Ltd v Yokogawa Australia Pty Ltd and Anor (No 7)*, the South Australian Supreme Court concluded that "unless qualified by its context, [consequential loss] would normally extend to all damages suffered as a consequence of a breach of contract". In *Regional Power*, Martin J rejects this approach as irrational, noting that "at its widest, the word consequential might always be read as somehow responsive to something, and thereby encapsulating almost every economic outlay, following upon a breach". In other words, 'consequential loss' has its natural and ordinary meaning, but not its widest natural and ordinary meaning.

In *Regional Power* itself, having decided that the meaning of 'consequential loss' is to be determined without further guidance on what the term might mean, Martin J is not wholly successful in deciding the issue on the facts without such further guidance. For example, his Honour seemingly endorses Ryan J’s formulation in *GEC Alstom Australia Ltd v City of Sunshine* that "the term consequential loss connotes a loss at a step removed from the transaction and its immediate effects" (italics added).

Advice for contracting parties

These cases highlight the difficulty facing contracting parties in this area. The practical application of a clause which simply excludes consequential loss is particularly uncertain in relation to commercial contracts containing numerous operative provisions, each creating different damages scenarios. For example, a single contract could give rise to loss for failure to deliver goods (or failure to deliver on time, or in specification), breach of intellectual property, breach of exclusivity and indemnity obligations for third party claims.

Until the High Court resolves this issue, parties are advised to clearly state the scope of damages that they intend to exclude, and define consequential loss if necessary. For example, a contract could exclude all loss other than that directly and naturally resulting in the ordinary course of events from the breach, which is the formulation stated in the *Sale of Good Act 1923* (NSW), and the first limb of *Hadley v Baxendale*. Alternatively, parties could adopt the Peerless approach. Although these approaches constitute a ‘construction predisposition’, they give the parties practical guidance.

Finally, if parties intend to exclude lost revenue or profits, or foregone business opportunities, whether direct or consequential, these should be stated separately to the language that excludes consequential loss.