TWENTY ESSEX

What counts as a claim for "loss of profits" – have exclusion clauses grown new teeth?

Henry Byam-Cook QC

CIS General Insurance v IBM [2021] EWHC 347 (TCC). Judgment of the English Technology and Construction Court, 19 February 2021.

Exclusions of "loss of profits"

Commercial disputes lawyers are familiar with clauses excluding liability for "loss of profits". These are regularly included in contracts in the energy, sale of goods, IT and shipping fields, and form part of the allocation of risk between the parties (especially in relation to complex projects). A recent decision by Mrs Justice O'Farrell in the Technology and Construction Court (TCC) suggests that such clauses may have considerably more bite than previously realised, excluding liability for claims for wasted expenditure under the "reliance loss" basis of damages. As such, the decision has potentially wide-reaching importance.

CIS General Insurance v IBM

The case concerned an IT implementation project. The judge held that CIS General Insurance Limited (CISGIL) had validly terminated the parties' Master Services Agreement on the basis of IBM's repudiatory breach. This left CISGIL without the new software system which it had contracted to receive. However, rather than claim damages assessed in the amount it would cost to obtain such a system from an alternative supplier, CISGIL claimed the sum of £128 million, being the wasted expenditure incurred on the project (covering the sums paid to IBM and sums paid to third parties in furtherance of the project).

IBM argued that this claim was excluded by a clause providing that "*...neither party shall be liable to the other... for any Losses...or for loss of profit... (in all cases whether direct or indirect)...*" on the basis that the claim for wasted expenditure was, on analysis, a claim for loss of profit. The judge accepted that submission.

She reasoned that claims for reliance losses are a species of claims for expectation losses, and are governed by the same over-arching compensatory principle which applies to claims for damages for breach of contract. In a commercial contract, the value of a party's expectation loss is usually measured by reference to the additional amount of money the claimant would require to achieve the financial value of the expected contractual benefit, such as lost profits. The fact that the claim is framed as one for reliance losses does not alter the analysis, a point confirmed by the caselaw holding that a claimant is not entitled to claim reliance loss damages if performance of the contract would have been unprofitable. In the case before her, she considered that the contractual benefit which CISGIL had

lost as a result of IBM's repudiatory breach comprised the savings, revenues and profits which would have been achieved had the IT solution been successfully implemented. A claim quantified in the amount of those lost profits would be excluded, and the re-framing of the claim as one for wasted expenditure did not change the characteristics of the losses for which compensation was sought. It was simply a different method of quantifying the same loss of bargain.

Lessons for the future

Claiming damages on the "reliance loss" basis is an important option for commercial disputes lawyers whenever faced with a case in which the calculation of damages is potentially complex, factually or evidentially. The effect of this recent decision is to threaten the prospects of such a claim whenever the relevant contract contains an exclusion for "loss of profits". It has, in that sense, significantly increased the effect of such exclusions and consequently altered the allocation of risk between the contracting parties.

It remains to be seen whether CISGIL will appeal the decision, but it seems likely given the amounts at stake. At the heart of the judge's reasoning is her view that the lost contractual benefit comprised the savings, revenues and profits which would have been achieved had the IT solution been successfully implemented. That view is open to challenge. Under the contract, IBM had promised to implement the IT solution and so what CISGIL had lost was an implemented, functioning IT solution. That in itself had a financial value (viz. the market cost for such an implementation) seperate from the profits which operating such system might have reaped in the period post-implementation.

This is a distinction which has been drawn in cases about the sale of goods. The courts have held that a claim for non-delivery of goods assessed on the contract versus market measure is not caught by an exclusion for "loss of profits" despite the fact that the buyer would have used the goods to make a profit by on-selling them (see, for example, *Glencore v Cirrus* [2014] 2 Lloyd's Rep 1 and *Scottish Power v BP* [2016] 1 All ER (Comm) 536). Put another way, the fact that a claimant cannot recover reliance losses if the contract would have proved loss-making if performed does not of itself mean that a claim for reliance losses is a claim for "loss of profits".

Read the full judgment

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Henry Byam-Cook QC

Henry practises in a range of commercial disputes, including fraud, shipping, energy and natural resources, IT and telecoms, banking and insurance. He has extensive experience of jurisdictional disputes and interim applications together with acting in trials, often in disputes with a complex, technical dimension and extensive cross-examination.

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