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Damages Waiver Clauses Often Problematic

By

Waivers of consequential damages in contractual agreements have become commonplace, yet these clauses often result in significant unintended consequences. Here is an example of a simple consequential damages waiver clause, the kind frequently found in the “miscellaneous” section of contracts:

Notwithstanding anything to the contrary contained in this Agreement, no party to this Agreement shall be liable for any consequential, special, indirect, incidental, exemplary or punitive damages of any kind or nature whatsoever, or any lost income or profits, regardless of whether arising from breach of contract or tort, even if advised of the possibility of such loss or damage or if such loss or damage could have been reasonably foreseen.

Clauses such as these have become commonplace and, therefore, may increasingly be viewed as merely boilerplate. Perhaps partly as a result of this perception, the mischief that can manifest from such clauses is frequently overlooked. There are any number of potential problems posed by the foregoing waiver provision that we will discuss in the future. For the purposes of this posting, we will concentrate on how the exclusion of lost profits from compensable damages can prove particularly problematic.

Consider the following example. Company “A” and Vendor “B” enter into a contract which outlines that software developed by B will be sold to A for a stated price. Upon delivery of the software, B bills A for the agreed price. Company A claims the software is defective and refuses to make payment; B files suit for damages equal to the contract price. The contract price, of course, includes B’s anticipated profit under the contract. However, the contract’s waiver of damages clause clearly states that “no party … shall be liable for any … lost income or profits ….” Has B waived any claim for the profits otherwise included in the contract price?

Lost profits in a breach of contract case may be consequential damages, but not necessarily. Some lost profits are “direct” damages. In the example above, lost profits are an intrinsic part of the contract, i.e., the payment to Vendor B under the contract includes the profit the vendor expected to make. B’s lost profits are a direct damage suffered by B. Yet, in the waiver clause above, consequential damages and lost profits are excluded – no distinction is made for lost profits that otherwise are included in the contract price. It would seem that B has waived its claim for lost profits, which typically are the only losses that would be sustained by B in a breach of contract case based on the facts presented.

This example suggests that contract counsel should resist broad undifferentiated references to “lost profits” in a waiver of consequential damages clauses. The better practice would be to carve out from such waivers direct damage lost profits that are inherent in the contract. An example of such a provision might read, “The foregoing provision shall not apply to amounts payable to Vendor B under [the payment provisions] of this Agreement.”

