Indemnification for Consequential Damages
By Marvin Garfinkel

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1. Introduction

This Attachment to the materials for the ALI-CLE Real World Document Drafting® Course of Study DRAFTING INDEMNIFICATION AND HOLD HARMLESS PROVISIONS considers the impact of various forms of waver of consequential damages provision in a contract or other document upon indemnification provisions of the same document or of another document to which such waver provision is applicable.\(^1\)

The waver of consequential damages provision might

(1) By its terms by specific reference or otherwise clearly (unambiguously) apply to an indemnification provisions of the same or a related document.

(2) Not specifically be made applicable to an indemnification provision but be held in litigation to be applicable to such provision,

(3) Be specifically made inapplicable to one or more particular indemnification provisions.- in the same or related documents

Or

(4) Although it does not directly address the issue be held on the basis of contract construction to be inapplicable to an indemnification provision in the same or related documents or both.

The failure of a waiver of consequential damage provision to deal with the issue of whether or not or to what extent the waver limits the application of an indemnification provision may be the result of the lawyers for one party or of both parties failing to identify the issue. Or, as is often the case in the negotiation of contract terms, the lawyer for one party may identify the issue but decide not to seek to resolve it with the lawyer for the other party or even alert the other party’s lawyer to the issue by including a resolution favorable to her client in a draft of the

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1 Although both the waver of consequential damage provision and the indemnification provisions being considered in this attachment will typically be in the same document the analysis should be equally applicable where they are in related documents as might be the case, for instance, where the waver of consequential damages is in a contract that is incorporated by reference into an merger agreement that contained the indemnification provision which by its terms is applicable to related contract’s such as those incorporated by reference.
document being negotiated for fear that the ultimate resolution of the issue in the final document will not favor her client.

A waver might by its terms be limited in its application to all or particular consequential damages or it might apply generally to consequential damages with exceptions that might be quite explicit or which might upon a claim being asserted require contract construction by a court or arbitrator to determine its extent and limitations.

I will in this attachment consider several situations described in this introduction.

2. Definition of Consequential Damages

In the pleading context, consequential damages are often referred to as “special damages.” Several commentators question whether the term “consequential damages” has a “clearly established meaning.” The terms are clearly intended to convey the concept of indirect rather then direct loss. As in a number of legal situations it is probably easier to describe the nature of direct damages and to indicate that any other loss will be considered to be consequential without reaching the issue of whether the damages are properly recoverable under particular circumstances. The term “consequential damages” has been defined in various ways for various purposes and in the context of different fact situations. It has been simply defined as "loss or injury that does not flow directly and immediately from a defendant's wrongful action but still occurs as a result or consequence of that action.”

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2 In Black & Veatch Construction, Inc. v. JH Kelly, LLC, 2011 WL 1706223 (US Dist Ct D. Oregon 2011) discussed at item 5 of this attachment the waver was by its terms made inapplicable to fraud or willful misconduct of the potentially indemnified party.


4 "Incidental Damages” may also be treated as a form of “special damages” although it is generally as provided for by §2-715 of the UCC generally considered to be a subset of direct or general damages,


6 Prof. Countryman added the footnote: “Obtain a large piece of stone. Take hammer and chisel and knock off everything that doesn’t look like an elephant.” to the textual statement :”Thus, by a process similar to one method of sculpting an elephant, we approach a definition of executory contract within the meaning of the Bankruptcy Act.” Vern Countryman, Executory Contracts in Bankruptcy Law: Part I, 57 Minn. L. Rev. 439 (1973).

7 See Hartford Accl. & Indem. Co. v. Case Found. Co., 10 Ill.App.3d. 115, 294 N.E.2d 7, 14, 92 A.L.R.3d 513 (1973). UCC §2-715(2)(a) states that “[c]onsequential damages resulting from the seller's breach include ... any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise.”