STEPHENSON HARWOOD

Offshore Energy Law

Are spread costs consequential loss?

The case of Transocean v Providence Resources arose out of a contract a contract for the hire of a semi-submersible drilling rig, 'GSF Arctic III'. The contract was on the LOGIC form and concerned the consequential loss clause. It will therefore be of interest to many active in offshore oil and gas.

Contrary to the terms of the contract the rig was not in good working condition on delivery due to a build-up of debris in a component of the blow-out preventer. The defect caused a loss of time of over 27 days. The dispute concerned the financial consequences of this delay.

Providence sought to recover its spread costs in the form of the costs of personnel, equipment and services contracted from third parties which were wasted as a result of the delay. Examples included well logging, well testing and cementing, mud engineers and mud logging services, geological services, diving and ROV services, weather services, directional drilling services, and running casings.

Transocean sought to defend the claim relying on the consequential loss clause which contained the usual mutual indemnity and hold harmless language and the following definition of consequential loss:

"Consequential Loss" shall mean:

(i) any indirect or consequential loss or damages under English law, and/or

(ii) to the extent not covered by (i) above, loss or deferment of production, loss of product, **loss of use (including, without limitation, loss of use or the cost of use of property, equipment, materials and services including without limitation, those provided by contractors or subcontractors of every tier or by third parties), loss of business and business interruption**, loss of revenue (which for the avoidance of doubt shall not include payments due to CONTRACTOR by way of remuneration under this CONTRACT), loss of profit or anticipated profit….."

The issue before the Court of Appeal was a short one: whether wasted spread costs incurred by Providence as a result of Transocean's breaches of contract were "consequential losses" within the meaning of the definition. The Court of Appeal, reversing the decision of Mr Justice Popplewell in the Commercial Court, held that they were and Providence's claim for its spread costs therefore failed.

In giving its judgement the Court of Appeal confirmed and clarified the following points of English law:

- The mutual indemnity clauses for consequential losses found in the LOGIC form are not simple exclusion clauses of a kind which the courts should construe restrictively in order to avoid commercial oppression.
- It was wrong to invoke the contra proferentem principle in this case. It is an approach to construction to which resort may properly be had when the language chosen by the parties is one-sided and genuinely ambiguous, that is, equally capable of bearing two distinct meanings.
- Since the decision in Photo Production Ltd v Securicor Transport Ltd [1980] A.C. 827 the courts have recognised that artificial approaches to the construction of commercial contracts are to be avoided in favour of giving the words used by the parties their ordinary and natural meaning.
- The principle of freedom of contract, which is still fundamental to our commercial law, requires the court to respect and give effect to the parties' agreement.

The Court of Appeal noted that the expression "consequential loss" has caused a certain amount of difficulty for English lawyers. The concept has given rise to a significant amount of cases and therefore case law. The Court of Appeal did not seek to follow that line of cases or seek to analyse whether the clause derogates from one or other or both limbs of the rule in Hadley v Baxendale (being the leading case law authority on consequential loss). Instead, the Court of Appeal identified the critical words to be those in bold underlined text and decided the case by placing primary importance on the language used.

The Court of Appeal held the language of the consequential loss clause was clear and was apt to exclude liability for wasted costs in the form of the spread costs which Providence seeks to recover in this case. Accordingly, Providence's claim failed.

The outcome is not surprising given the language in the clause and the Court of Appeal's guidance should be helpful in preventing and resolving future disputes. Care should be taken however, as not all of the LOGIC standard contracts use all of the language that the Court of Appeal considered to be "critical" in this case.

Accordingly, the issue of whether spread costs are consequential losses is not finally resolved by this case; it all depends on the wording. If parties wish to include spread costs within the concept of consequential loss it would be appropriate to have close regard to the definition of consequential loss used in this case.

Simon Moore
Partner, London
T: +44 20 7809 2164
E: simon.moore@shlegal.com

Simon specialises in contentious and non-contentious matters in the offshore oil and gas and insurance industries.

He has advised on offshore oil and gas projects and conducted litigation and arbitration around the world. Projects Simon has acted on include, Kwame Nkrumah FPSO (Ghana), Benguela-Belize CPT (Angola), BP Thunder Horse (GoM), BP Mad Dog (GoM), BP Mad Dog 2 (GoM), Agbami FPSO (Nigeria), Usan FPSO (Nigeria), Senje Berge FPSO (Nigeria), Akpo FPSO (Nigeria), Coral FLNG (Mozambique), Pazflor FPSO (Angola), Frade FPSO (Brazil), Icthys FPSO (Australia) and Balder FPSO (North Sea).

Simon successfully acted for the underwriters in the marine insurance case the "*B Atlantic*" before the UK Supreme Court in May 2018 and was awarded the Solicitor of the Year Award (Private Practice) by the Law Society in October 2018.

Simon is co-author of the leading text on law and practice relating to design and construction of vessels for offshore oil & gas: Offshore Construction Law and Practice, published by Informa Law for Routledge.

Simon also authored the Decommissioning Contracts chapter in the text, Oil and Gas Decommissioning: law policy and comparative practice (Second Edition), published by Globe Law and Business.

STEPHENSON HARWOOD