

Lost Profits: Direct or Indirect Damages?

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In 2014, the New York Court of Appeals, in *Biotronik A.G. v. Conor Medsystems Ireland, Ltd.*, held that the lost profits claimed by a party were “general damages”, and were recoverable. They were recoverable despite the limitation of liability provision in the contract, which stated that neither party would be liable for “any indirect, special, consequential, incidental or punitive damage with respect to any claim arising out of [the] agreement” for any reason, including a party’s performance or breach of the agreement.

Why is a case that was decided in 2014 worthy of writing about now? It’s been over three years since the Court’s decision, and we still commonly see limitation of liability language in commercial contracts that does not clearly address the issue of lost profits, and whether they are direct or indirect damages. That may be a strategic decision of the drafter, or it may be an oversight. While New York law does not govern all commercial contracts, other courts may rely on *Biotronik* in the future, or reach a similar holding independently. Regardless, it’s generally better to have a contract that clearly expresses the intent of the parties, rather than have a court determine it.

Direct Damages vs. Indirect Damages

Consider whether lost profits are reasonably foreseeable and quantifiable. Will breach of the contract almost surely cause a party to lose profits? Is there a reasonably certain way to prove the amount of lost profits? If so, lost profits may be considered direct damages. For example, if the parties have a

non-compete agreement, the main purpose of that agreement is to ensure one party does not compete with the other party for business, thereby diverting customers, which results in lost profits. Lost profits can be reasonably quantified by sales to each diverted customer by the competing party. This is a situation where lost profits would likely be considered direct damages.

Defining Lost Profits

Consider whether the parties want lost profits to be recoverable. A provision can be included in the contract expressly stating that lost profits are direct damages, or that lost profits are indirect damages. Limitation of liability language can be included that states lost profits are not recoverable, regardless of how they are categorized. Alternatively, the limitation of liability language can expressly exclude lost profits from the limitation, making them recoverable.

Ultimately, whether lost profits should be recoverable, and how they are addressed in a contract will depend on the individual relationship or transaction in question. Given the potential for dispute, drafting clear language is key.

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