Concentrate Questions and Answers Contract Law: Law Q&A Revision and Study Guide (3rd edn)

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11. Damages

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Abstract

The *Concentrate Questions and Answers* series offers the best preparation for tackling exam questions. Each book includes typical questions, answer plans and suggested answers, author commentary, and other features. The common law places great emphasis on damages as the primary remedy for breach of contract, reinforced by the fact that although a victim of a breach may seek specific performance or an injunction, such orders are equitable in nature and therefore discretionary. In claiming damages, the victim of a breach will need to establish that: the claimed method for assessing damages is appropriate (measure); the damages are not too remote (remoteness); if relevant, compensation for inconvenience and/or disappointment caused by the breach is recoverable (non-pecuniary losses); the losses could not have been reasonably mitigated (mitigation); and the recoverable losses have been properly quantified (quantification). Separately, the validity of any agreed damages clause will need to be determined.

Keywords: breach of contract, remedies, loss of bargain, expectation loss, remoteness, non-pecuniary, mitigation, penalty clause

Are you ready?

In order to attempt the questions in this chapter you must have covered the following areas in your revision:

- The generally compensatory nature of damages;

- The nature of loss;
- The appropriate measure of damages—for example, the difference between expectation and reliance losses;
- The availability of damages for non-pecuniary losses;
- Remoteness of damage;
- Mitigation of loss;
- The difference between an agreed or liquidated damages clause and a penalty clause.

Key debates

Debate: the meaning of loss.

What is the difference between expectation and reliance losses? To what extent is there flexibility in identifying loss (as in a case such as ***Wrotham Park Estate Co. Ltd v Parkside Homes Ltd*** which was more recently discussed in ***Morris-Garner v One Step (Support) Ltd*** **[2018] UKSC 20**)? To what extent does the law allow damages to be recovered for inconvenience, distress, injury to feelings, or other non-pecuniary losses?

Debate: the rule of remoteness.

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There are uncertainties surrounding the operation of the rule of remoteness in ***Hadley v Baxendale*** and further uncertainty has been created by ***Transfield Shipping Inc. v Mercator Shipping***, ↵ which may require an assumption of responsibility for loss to be recoverable. Interestingly, more recently in ***Attorney General of the Virgin Islands v Global Water Associates Ltd*** **[2020] UKPC 18 at [26]** the Privy Council was keen to stress that the case before it was not concerned with 'unusual volatility in the market or questions of market understanding' as in ***Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)***.

Debate: penalty clauses.

In ***Makdessi v Cavendish Square Holdings BV*** the Supreme Court considered the operation of the penalty rule, the first time the Supreme Court (or House of Lords) had done so in a century. In that case the Supreme Court restated the principles used to distinguish penalty clauses from liquidated damages clauses. To what extent did this restatement alter traditional principles?

Question 1

Jack is a manufacturer and seller of frozen food. Botchit & Co. agree to lay the floor in Jack's newly constructed factory, the work to be completed on 1 April at a cost of £25,000. Clause 12 of the contract provides: 'If Botchit & Co. fail to complete the contract within the stipulated time, we undertake to pay, by way of penalty, a sum of £10,000 in full satisfaction of our liability.'

Jack also enters into a contract with Marko & Co. to install machinery in his factory (5–14 April), for the purposes of converting fresh food into frozen, at a cost of £750,000. Botchit & Co. is informed of Jack's contract with Marko & Co.

Jack intends to commence production of frozen food on 15 April and, in consequence, he enters into a contract with Fatts Ltd for fresh food to the value of £200,000 to be delivered to the factory on 14 April.

Botchit & Co. only complete the floor on 8 April. As a result, Jack decides to pay Marko & Co. an extra £50,000. This sum of money is intended to cover overtime payments for Marko's employees caused by the shortened time for completion, thus enabling the machinery to be installed by 14 April. Whether Marko & Co. was contractually entitled to any compensation remains unclear. Jack finally commences frozen food production on 18 April. Unfortunately, the fresh food that had been delivered by Fatts Ltd on 14 April had to be sold off by Jack for £10,000 to local pig farmers.

Advise the parties.

Caution!

■ Nearly all problem questions involving damages require you to adopt the same structure: was there a breach of contract? If there was a breach of contract, is there a valid damages clause? If there is not a valid damages clause, how are damages measured? What losses were caused by the breach? Are any losses too remote? Can damages for any non-pecuniary losses be awarded? What steps were taken to mitigate losses?

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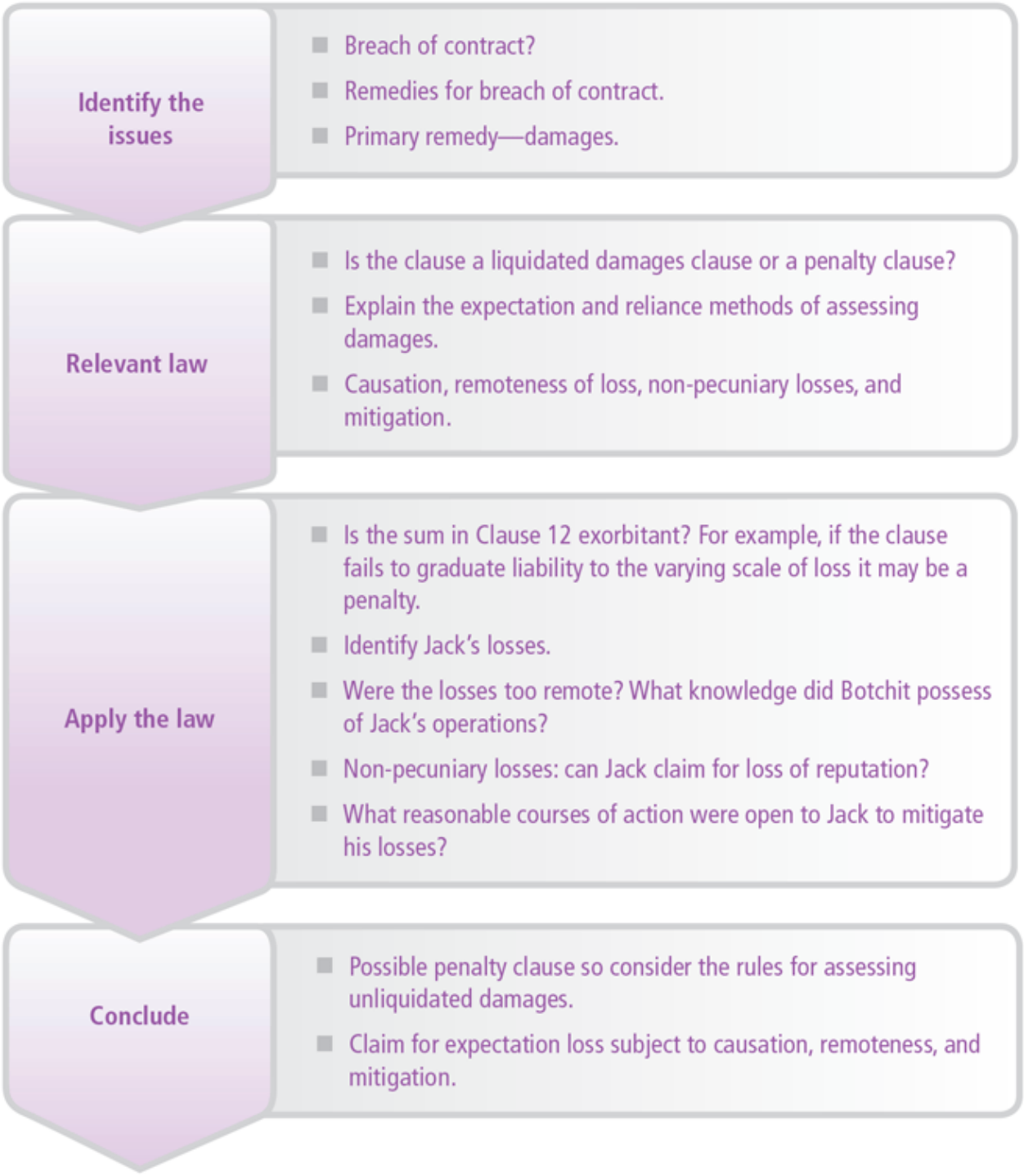
■ This represents the archetypal damages question. It contains the main ingredients of the law relating to damages: causation, remoteness, mitigation, and agreed damages clauses. Note that if an agreed damages clause is valid, then a claimant cannot claim unliquidated damages at common law.

Diagram answer plan



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Suggested answer

This question concerns breach of contract and remedies for breach of contract, particularly damages. Damages may be assessed by the courts or may be agreed in advance by the parties in the form of an agreed damages clause.[1] The difficulty in predicting the damages recoverable for a breach of contract often encourages the parties to insert an agreed damages clause into the contract, thereby obviating the need to go to court. Should a clause, rather than leaving damages to be assessed at common law by the courts, provide a contractual remedy (this is a secondary obligation) on breach of a contract obligation (the primary obligation), then it will be subject to control by the courts through the penalty rules: ***Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67**.[2] If, as seems to be the case, Botchit & Co are in breach of contract, is the clause 12 a penalty clause?

[1] This outlines the subject of the question and raises the two main issues to be addressed.

[2] This sentence indicates the 'policing' of agreed damages clauses through the penalty rules and provides a link to the restatement of the law in this area by the Supreme Court.

Agreed Damages Clause

Following the ***Makdessi v Cavendish Square Holdings BV*** case, the test is whether the clause (as a secondary obligation) 'imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation' (Lord Neuberger).[3] An assessment must be made of what is a legitimate interest and whether the contractual remedy is out of all proportion to that interest. Punishment of a contract-breaker is not a legitimate interest but compensation for a breach will amount to a legitimate interest. Is the clause in the contract a penalty and unenforceable, essentially allowing the court to award damages in accordance with the normal rules of contract damages; or is it a liquidated damages clause, which means the common law rules (eg remoteness) are disregarded and the parties can rely on their agreed remedy in the event of the specified breach?

[3] The test for establishing the existence of a penalty clause is explained although note in ***CFL Finance Limited v Jonathan Bass* [2019] EWHC 1839 at [48]** Judge Briggs stated: 'There is little guidance on what may constitute a legitimate interest, save that there can be no legitimate interest in punishing the defaulting party.'

In ***Dunlop Pneumatic Tyre Co. v New Garage and Motor Co. Ltd*** **[1915] AC 79** the following guidelines were formulated by the House of Lords (guidelines which, in many cases, continue to be helpful after ***Cavendish Square Holings BV v Makdessi***).[4] First, the clause will be considered penal if the sum stipulated is extravagant or unconscionable in comparison with the greatest conceivable loss which could arise. Consequently, as recognized in ***Murray v Leisureplay plc*** **[2005] EWCA Civ 963, [2005] IRLR 946**, the recovery of a sum greater than the actual loss suffered does not inevitably lead to the clause being deemed penal in nature. On the facts, Botchit is expected to pay Jack £10,000 for the delay. It is arguable that this is not an exorbitant sum, bearing in mind the expected loss of production and the dislocation of other arrangements caused by significant delays.

[4] This paragraph explains how to distinguish a penalty clause from an agreed damages clause.

p. 182 ↵ Secondly, the clause is normally a liquidated damages clause if the consequences of the breach are such as to make precise pre-estimate impossible and the actual amount specified bears a reasonable relation to the probable consequences of the breach (see the facts of ***Dunlop v New Garage***). Superficially, it appears difficult to estimate the real loss resulting from delay. On the other hand, the specified sum is not graduated in accordance with the severity of the breach. For example, the loss sustained by Jack might be minimal if Botchit & Co. delayed by only one day but it might be considerable if the delay exceeded two months. Thus, the clause is arguably not linked to any legitimate interest of Jack and so could be considered a penalty clause.[5]

[5] As it is concluded that the clause *may be* a penalty this allows consideration of how the courts would assess damages for Botchit's delay.

On the basis that the damages clause is penal, the court will have to assess Jack's actual losses under the normal common law rules of recovery. At common law the purpose of damages is usually to compensate the victim for the loss caused by the defendant's breach of contract, rather than to punish the defendant, in this case Botchit & Co.[6]

[6] An explanation of the nature of damages at common law is provided.

Measure

Presumably Jack will want to claim 'expectation' damages equivalent to being put in the position he should have occupied if the contracts had been properly performed (see ***Robinson v Harman* (1848) 1 Ex 850**). More specifically, Jack will want to claim any lost profits resulting from the delay in commencing production, the loss incurred in selling off the fresh food consignment as pig food, and the additional payment of £50,000 to Marko & Co.[7] The first question, therefore, is whether these losses were caused by Botchit and Co.'s breach (we are not, for example, informed why, after the additional payment to Marko & Co., production did not commence until 18 April). The second question is whether these losses are too remote.

[7] The good student *might* also consider the loss to Jack's reputation—see later section on 'Non-Pecuniary Losses'.

Remoteness

The basic principle in ***Hadley v Baxendale* (1854) 9 Exch 341** states that losses are too remote if, at the time of the contract, they were not in the reasonable contemplation of the parties as liable to result from the particular breach.[8] The courts will have to consider a number of questions in deciding the issue of remoteness. For example, as Botchit & Co. knew about the anticipated installation of machinery by 14 April, a court might conclude that Botchit & Co. had implicitly accepted liability for any production delays suffered by Jack as a consequence of the late completion of the factory floor, although whether knowledge of the facts should *always* be equated with acceptance of loss where the contract is broken remains a moot point ↵ (compare ***Transfield Shipping Inc. v Mercator Shipping Inc., The Achilleas* [2008] UKHL 48, [2008] 4 All ER 159**, ***Sylvia Shipping Co. Ltd v Progress Bulk Carriers Ltd (The Sylvia)* [2010] EWHC 542 (Comm), [2010] 2 Lloyd's Rep 81** and ***Attorney General of the Virgin Islands v Global Water Associates Ltd* [2020] UKPC 18**). Conversely, if Botchit & Co. was not aware that Jack was intending to start production from 15 April, would any loss of profits resulting from the delay have been reasonably contemplated? Support may be found in ***Hadley v Baxendale*** where the carrier was not expected to foresee the consequences of his delay as the mill owner failed to inform him of the absence of any spare shaft.

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[8] This paragraph illustrates IRAC. The issue is that of remoteness, the concept is explained, applied, and arguable conclusions reached. In ***Attorney General of the Virgin Islands v Global Water Associates Ltd* [2020] UKPC 18** the Privy Council were of the view (at **[32]**) that '[t]o be recoverable, the type of loss must have been reasonably contemplated as a serious possibility…'.

Moreover, the ability of the defendant to foresee possible losses may arise from the capacity in which he contracted. For example, in ***The Heron II*** **[1969] 1 AC 350** the shipowners were expected to know of the fluctuating prices on the commodity markets. It was, therefore, within their reasonable contemplation that a delay might cause loss to their clients if the market price moved against them. Equally, if Botchit & Co. are experienced builders they might be expected to predict more accurately the consequences of their actions. As a factory floor is often laid as a precursor to the installation of machinery, any delay in completion might foreseeably cause a consequential delay to that installation.

As all these issues raise questions of fact, it is difficult to come to a specific conclusion. However, in practice, it is arguably likely that the loss caused by a delay in commencing production seems the most foreseeable as Botchit & Co. must realize that Jack is a frozen food manufacturer who wishes to utilize his assets (factory) as quickly as possible. The claim for overtime payments is potentially dependent upon the success of the first claim: if the delay in frozen food production was too remote, surely an additional payment to a third party to ensure timely installation of the production machinery would be equally remote? However, Jack's counsel will refer to ***John Hunt Demolition Ltd v ASME Engineering Ltd*** **[2007] EWHC 1507 (TCC), [2008] 1 All ER 180** which suggests that the payment to Marko & Co. will be recoverable from Botchit & Co. provided it is viewed as a 'reasonable settlement' by the court—such reasonableness potentially being established even though the legal enforceability of that payment was questionable. As Botchit & Co. was aware of the tight deadline for installation of the machinery by Marko, a court may conclude that the overtime payments that were made were reasonably foreseeable under the second branch of the ***Hadley v Baxendale*** remoteness principle. Finally, the sale of the fresh food seems the most remote as it requires Botchit & Co. to foresee the possibility of Jack organizing a consignment of food before the works had

p. 184 ↵ definitely been completed and the potential consequences of food storage facilities being unavailable.

Non-Pecuniary Losses

In relation to non-pecuniary losses,[9] one might consider the possible impact of delay on Jack's reputation. Generally, damages for injured reputation are difficult to recover in the law of contract, especially as the law of tort offers remedies in defamation and malicious falsehood. But there are exceptions. In particular, it may be possible to claim damages for injury to commercial reputation, for example see ***Anglo-Continental Holidays Ltd v Typaldos Lines (London) Ltd*** **[1967] 2 Lloyd's Rep 61**. Jack's reputation might also suffer if he has entered into contracts to supply frozen food to certain customers by a particular date. However, it is submitted that Jack would fail in such a claim as these losses would be considered too remote.

9 The claim relating to non-pecuniary loss is difficult to argue so the answer raises the possibility but deals with the issue briefly.

Mitigation

Jack has a 'duty' to mitigate[10] any loss. A court will not expect him to take the *most* reasonable course of action or explore every avenue in order to minimize his losses. Rather, he must adopt a reasonable course of action. Presumably, Jack must have known by 2 April that Botchit & Co. would not be completing on time. Should (and could) he have contacted Fatts Ltd and delayed delivery until he was confident that his processing plant would be operational by a specific date? Ought he to have considered temporary storage of the fresh food, assuming that such facilities were available? Could he have obtained a better price for the food? If an affirmative answer to *any* of these questions is forthcoming, it will raise serious doubts as to whether Jack's course of action could be regarded as 'reasonable'. Alternatively, if the court decided that such actions involved too much practical inconvenience for Jack, then such possible courses of action would be ignored (see, generally, ***Pilkington v Wood*** **[1953] Ch 770**).

10 Mitigation is another key issue in relation to damages. IRAC again may be used in relation to this issue.

Looking for extra marks?

■ Explain the nature of damages, especially the purpose of damages for breach of contract. An explanation of the relationship between unliquidated damages and liquidated damages; that is the relationship between the common law rules on damages and the parties determining damages for themselves in an agreed damages clause.

■ The penalty clause jurisdiction of the courts following the decision of the Supreme Court in ***Cavendish*** could be explained further.

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Question 2

Deco Ltd purchased an eighteenth-century property to be used as its new business premises from 19 April. The property needed to be completely repainted and have a central heating system installed. Deco Ltd hired Jerry for the sum of £1,000 to do the painting, all work to be completed by 18 April otherwise a deduction of 5 per cent in the contract price would be made for each day that completion was delayed. Deco Ltd also purchased a new heating system from Warmwall & Sons. The contract stipulated that the system needed to be installed by 18 April, with Warmwall & Sons being required 'to pay £1000 by way of penalty to Deco Ltd for any late completion of the work'.

Jerry did not complete the work until 28 April (ten days late). This meant that Deco Ltd was unable to operate normally from its new premises until 29 April, causing an approximate loss of profits in the region of £500 per day (from 18 April).

Coincidentally, the heating system was not fully installed until 28 April, so Deco Ltd was required to hire six portable electric heaters as the house was cold and damp—total hire charge and electricity was approximately £150 per day, for ten days. Moreover, two days later, owing to a gas leak, the heating system exploded, causing severe structural damage to the property and ruining an antique tapestry which had recently been acquired by Deco Ltd for hanging within its client reception area.

Advise Deco Ltd.

Caution!

■ As mentioned earlier, consider adopting a simple structure to your answer: breach, impact of agreed damages clause, causation, remoteness, special types of damages, and mitigation.

■

When considering agreed damages clauses, be careful about concluding that the clause is *definitely* valid as this may leave very little left to write about.

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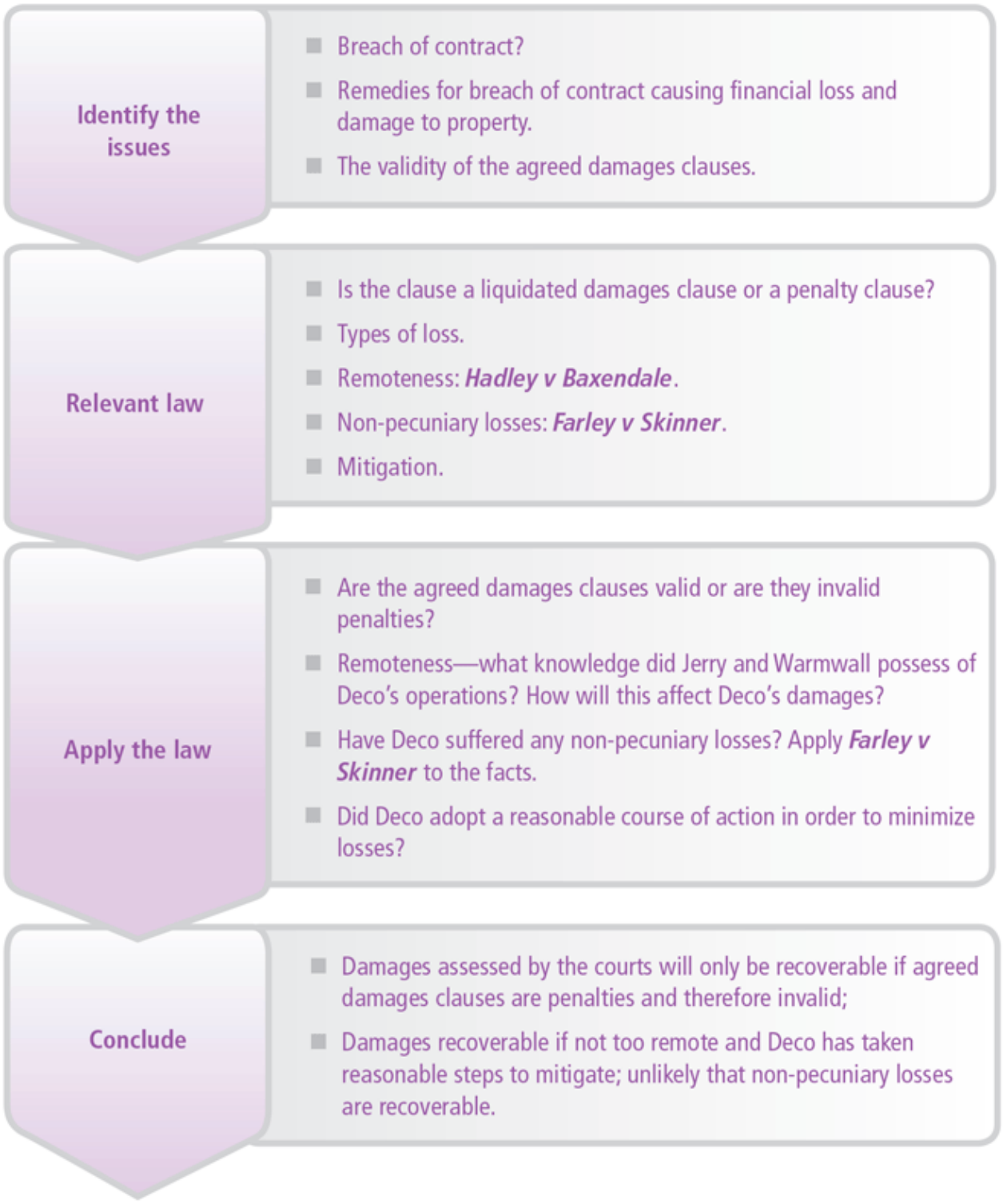
Diagram answer plan



Suggested answer

The question concerns damages for breach of contract. The facts disclose that the contracts between Deco and Jerry and between Deco Ltd and Warmwall & Sons have been broken. Both Jerry and Warmwall had promised to finish the work by 18 April and by failing to complete on time are in breach, being strictly liable. Moreover, in the contract between Deco and Warmwall, in the absence of express provision, there will be an implied term that Warmwall will take reasonable care ↵ and skill in providing the service. If the gas leak is Warmwall's fault, then there will be a breach of this term. Deco, as the victim of these breaches of contract, has suffered a loss of profits as well as damage to its property. A victim's first decision is to choose whether to claim damages for expectation loss ('loss of bargain'),[1] putting it in the position it should have occupied if the contract had been performed correctly (see ***Robinson v Harman* (1848) 1 Ex 850**), or 'reliance losses', representing compensation for any out-of-pocket expenses and costs associated with performance,[2] as well as placing it back in the position it occupied before the contracts had been concluded (see ***McRae v Commonwealth Disposals Commission* [1951] 84 CLR 377**). Presumably Deco Ltd will wish to claim his expectation loss from Jerry so as, for example, to recover lost profits. Deco may also wish to claim expectation loss from Warmwall & Sons in respect of the loss which should have been avoided.

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[1] The answer identifies damages as a key subject for discussion and explains the nature of loss of bargain damages.

[2] Shows an understanding of an alternative measure of loss, ie reliance interest.

Agreed Damages Clauses

However, Deco may not be able to claim damages for its actual loss, if the agreed damages clauses in its contracts with Jerry and Warmwall are valid and not penalty clauses.[3] In ***Makdessi v Cavendish Square Holdings BV* [2015] UKSC 67** Lord Neuberger said the test for a penalty clause is whether the clause (as a secondary obligation) 'imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation'. In applying this test to a straightforward damages clause where the interest is merely compensation for breach, reference may be made to ***Dunlop v New Garage and Motor Co. Ltd* [1915] AC 79**. In this case Lord Dunedin established a number of guidelines[4] including: if the sum stipulated is extravagant or unconscionable in comparison with the greatest conceivable loss, it is a penalty clause; and where a single fixed sum is payable on the occurrence of varying events, necessarily causing different amounts of loss, the presumption is that it is a penalty clause. At first glance the sums of money mentioned in either clause do not appear to be unduly extravagant. However, Jerry might be deprived

of any payment if he is more than 20 days late. Is this out of proportion to Deco's legitimate interest; that is, compensation? If yes, then it is a penalty clause and unenforceable—requiring the court to apply the normal common law rules regarding the recovery of damages.

[3] This sentence indicates to the examiner that you are aware of the relationship between an agreed damages clause and damages assessed by the courts at common law.

[4] The relevant guidelines are stated and then applied to the facts of the question.

Secondly, although both sums of money are payable for one particular type of breach, the clause in Warmwall's contract does not appear to graduate its liability. Whether Warmwall completes one hour late or one year late seems to make no difference: the same amount of money is payable. Thus, under the guidelines in ***Dunlop***, it might be ↵ difficult to argue that the sum of £1000 bears a reasonable relation to the probable consequences of the breach. As already noted, this would make the clause penal in nature, again requiring the court to resort to the normal common law rules on recovery.

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Remoteness

On the basis that these clauses are arguably penal in nature, we will need to consider the normal common law rules on damages. In particular, Deco Ltd will need to identify each loss suffered, establish that it was caused by the breaches, and that it was not too remote[5] from Jerry or Warmwall's breaches of contract; that is, that there is a sufficiently strong causal connection between the breach of contract and the claimed loss. Adopting the principle first stated by Alderson B in ***Hadley v Baxendale* (1854) 9 Exch 341**, damages are only recoverable if: (a) they are fairly and reasonably considered to arise naturally from the breach; or (b) they were in the contemplation of the parties at that time of contract formation as liable to result from the breach.[6] This offers a single test for awarding damages for breach of contract based on the 'reasonable contemplation' of the parties, the level of liability depending upon the degree of knowledge possessed by the contract-breaker.

[5] This sentence identifies an issue.

[6] Here there is a clear statement of the rule relevant to the issue. Note that in ***Attorney General of the Virgin Islands v Global Water Associates Ltd*** **[2020] UKPC 18** the Privy Council were of the view (at **[32]**) that '[t]o be recoverable, the type of loss must have been reasonably contemplated as a serious possibility…'.

Clearly Jerry and Warmwall & Sons have been asked to complete their respective contractual duties by 18 April. As traders they must encounter many situations where time limits are imposed and, consequently, late completions will inevitably cause their customers some inconvenience. However, Deco's losses generally result from the need to occupy and operate from their premises from 18/19 April. Was this known to Jerry and Warmwall & Sons and also that delays in completion might prevent Deco from opening for business? Perhaps Deco can rely on the first branch of the remoteness principle set out in ***Hadley v Baxendale***;[7] namely, that the losses were fairly and reasonably considered to arise naturally from the breach (ie delayed completion prevented occupation of the premises for business purposes). However, in ***Hadley v Baxendale*** the court decided that the mill owner's failure to inform the carrier of the absence of a spare shaft prevented him from claiming any loss of profits resulting from the delayed return of the repaired shaft. Surely any failure by Deco to inform either party of its intention to use the offices from 19 April would be treated similarly? Moreover, has either set of contractors assumed responsibility for such loss[8] (see ***Transfield Shipping Inc. v Mercator Shipping Inc., The Achilleas*** **[2008] UKHL 48, [2008] 4 All ER 159** and ***Siemens Building Technologies FE Ltd v Supershield Ltd*** **[2010] EWCA Civ 7, 129 Con LR 52**; cf ***Sylvia Shipping Co. Ltd v Progress Bulk Carriers Ltd (The Sylvia)*** ↵ **[2010] EWHC 542 (Comm), [2010] 2 Lloyd's Rep 81** and ***Attorney General of the Virgin Islands v Global Water Associates Ltd*** **[2020] UKPC 18**)? Alternatively, what if Jerry and/or Warmwall had been notified of the consequences of late completion?[9] Applying the second branch of the rule in ***Hadley v Baxendale***, this would prove that the consequences of late completion were reasonably contemplated. Whilst this would not necessarily prove that either of the builders had accepted liability for such losses, following ***John Grimes Partnership Ltd v Gubbins*** **[2013] EWCA Civ 37, [2013] BLR 126**, a court might imply a term to such effect, provided circumstances did not suggest otherwise.

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[7] The answer considers the application of the first branch of the rule in ***Hadley v Baxendale***.

[8] The answer acknowledges the uncertainty in the law following the decision in ***The Achilleas***.

[9] Here there is an application of the second branch of the rule in ***Hadley v Baxendale***; which completes IRAC in this paragraph.

The damage caused by the gas leak offers interesting possibilities. Assuming that Warmwall & Sons caused the leak, and that Deco Ltd was not expected to have been checking for such problems (compare this with ***Beoco Ltd v Alfa Laval Co. Ltd* [1994] 4 All ER 464**), it would seem that the two rules in ***Hadley v Baxendale*** would cover the situation. The only issue would be whether the purchase of the antique tapestry, *after* the contract with Warmwall had been entered into was a relevant consideration. Is it likely that gas leaks will cause damage to any artefacts stored on premises and that Deco, as a company, might well have expensive ornaments in order to impress its clients? Arguing that Warmwall should have been told the value of the precise items on the premises as a pre-condition of liability would appear needlessly burdensome for Deco.

Non-Pecuniary Losses

Apart from the normal pecuniary loss, it seems unlikely that Deco Ltd could recover any other special damages. The main objects of the contract are all business-related.[10] It may well be that the owners of Deco Ltd will be 'disappointed' by the delays but that is insufficient. In ***Bliss v SE Thames Regional Health Authority* [1987] ICR 700** it was clearly stated that such damages were irrecoverable in an arm's-length commercial contract, although certain *obiter* comments in ***Farley v Skinner* [2001] UKHL 49** would suggest that the distinction between 'business' and 'non-business' contracts should not be the critical determinant in such circumstances. Similar reasoning could be used as regards any physical inconvenience suffered by Deco employees. Presumably, the purpose of the contract is primarily to enhance the earnings potential of Deco Ltd, not to improve the working environment of its employees.

[10] The loss suffered depends upon what has been promised under the contract and also what the law allows to be claimed.

Mitigation

To what extent would Deco Ltd be expected to mitigate its losses? It will only be expected to act reasonably, rather than taking the most reasonable course of action. In relation to the breach of contract by ↵ Jerry, could Deco have stayed at its old premises for another few days, or was the move irreversible? Was alternative accommodation available or would the inconvenience and disruption caused to Deco make that option unreasonable? In relation to the breach of contract by Warmwall & Sons, the hire of portable heaters at that cost seems extravagant. What other options did Deco Ltd consider and with which other suppliers did it communicate?[11]

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[11] The purpose of posing such questions is that it demonstrates to the examiner an understanding of how the rules of mitigation would be theoretically applied by a court.

Looking for extra marks?

■ Clearly you cannot always predict the decision of the court on any issue involving a question of fact. What is important is that you state the law accurately, identify any specific problems, and make several remarks on how the law might sensibly be applied to the facts.

■ Indicate where there are uncertainties in the law and how this may impact upon your answer. For example, consider the differences in relation to remoteness apparent in the cases of ***Parsons Ltd v Uttley Ingham Ltd*** **[1978] QB 791** and ***Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*** **[1949] 2 KB 528**.

Question 3

The overriding principle in the award of damages for breach of contract is that the victim should be fully compensated for all the losses which flow from that breach.

Discuss.

Caution!

■ The mere regurgitation of lecture notes must be avoided and an attempt made to answer the question (for example, you might identify particular situations where the claimant's actual losses are not fully recoverable).

■ The answer adopts one of many possible structures. You might also consider other aspects, such as the basis upon which damages are awarded (eg compare reliance and expectation losses), or problems over the meaning of loss as seen in ***Ruxley Electronics and Construction Ltd v Forsyth*** **[1996] AC 344**, or the quantification of loss (eg non-delivery of goods which thwarts a profitable sub-sale by the buyer), or the enforceability of agreed damages clauses which may not fully compensate the victim of a breach.

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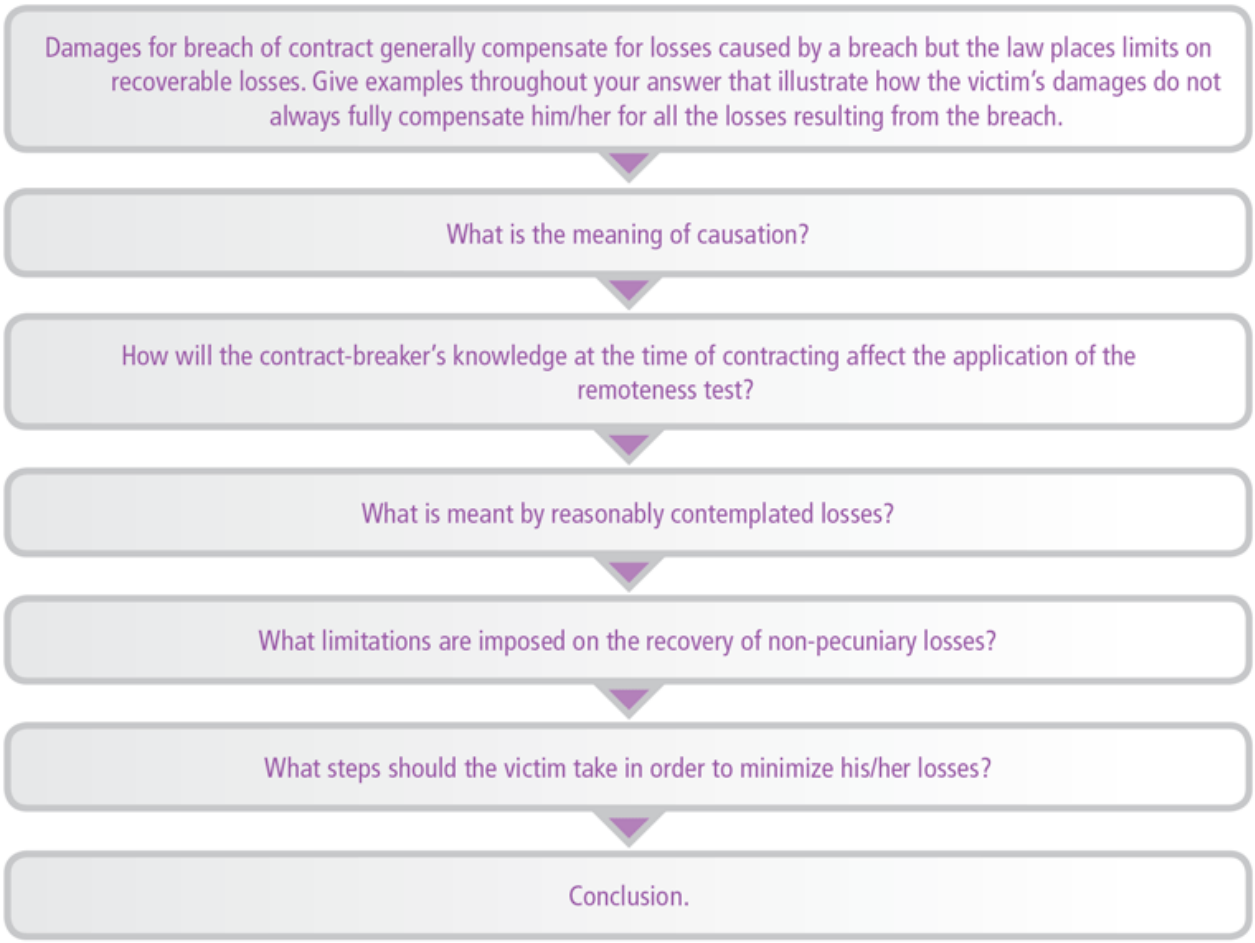
Diagram answer plan



Suggested answer

The purpose of awarding damages for breach of contract is generally to compensate the claimant rather than punish the defendant, thereby excluding the award of exemplary damages.[1] Thus, although damages can be claimed as of right by the victim of a breach, such damages may only be nominal, substantial damages requiring proof that actual losses were sustained as a result of the breach. Where the claimant has suffered no loss, he/she will not normally be awarded substantial damages even if there is proof that the defendant's breach was committed deliberately and with a view to profit, unless the court is prepared to disguise such an award under the general heading of injury to the claimant's feelings (eg ***Cox v Phillips Industries Ltd*** **[1976] 1 WLR 638** but compare ***Bliss v SE Thames Regional Health Authority*** **[1987] ICR 700**). The general aim of damages is to compensate the claimant for a loss suffered.

[1] As the question concerns damages, an explanation of the nature and purpose of damages should be given.

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↵ However, three questions emerge from the quotation.[2] How does one assess whether the loss suffered is actually *caused* by the breach? Is the recovery of damages based upon an assessment of the direct consequences of the breach or is it limited by a test of foreseeability? Finally, will the victim be fully compensated for *all* the losses suffered?

[2] By identifying sub-questions within the overall question, a structure for your answer may be created.

Causation

There must be a sufficiently strong causal connection between the loss suffered and the actual breach.[3] In this context, causation is not exclusively subsumed within the remoteness principle. For example, if the breach of contract is one of two causes for the loss suffered, both causes acting concurrently, then a court may still award normal damages (see ***Heskell v Continental Express Ltd* [1950] 1 All ER 1033**). Thus, in ***Smith, Hogg & Co. v Black Sea Insurance Co. Ltd* [1940] AC 997**, the cargo was lost because of bad weather and also because, in breach of contract, the ship did not fulfil the seaworthiness criterion. It was held that the breach was sufficient to support a claim for damages. However, if the bad weather had been so extreme that no ship would have survived, then damages might not have been recoverable. In this way, the principle of causation ensures that the claimant does not recover for losses under the notional pretext that a breach has occurred.

[3] This paragraph employs PEA. The first sentence explains the *point*, the next lines explain the law (providing *evidence*), and the final sentence offers *analysis* in applying it to the question.

Remoteness

The principle of remoteness limits the recovery of losses directly caused by the breach. The courts have traditionally adopted a test which limits recoverable loss to that which was in the reasonable contemplation of the parties as liable to result from the particular breach (see ***Hadley v Baxendale* (1854) 9 Exch 341** and ***The Heron II* [1969] 1 AC 350**). In ***Attorney General of the Virgin Islands v Global Water Associates Ltd* [2020] UKPC 18** the Privy Council were of the view (at **[32]**) that '[t]o be recoverable, the type of loss must have been reasonably contemplated as a serious possibility…'.

The knowledge of the parties is the determining factor and can be illustrated by a comparison of the following cases. In ***Diamond v Campbell-Jones*** **[1961] Ch 22** the defendant, in breach of contract, refused to sell a house to the plaintiff. The defendant knew that the plaintiff was a dealer in real property but not that he intended to convert the premises into offices and flats. It was held that, as the defendant did not possess any knowledge of the plaintiff's specific intentions, he was not liable for the loss of redevelopment profits. Conversely, in ***Cottrill v Steyning & Littlehampton Building Society*** **[1966] 1 WLR 753**, the vendor of a hotel knew that the purchaser intended to convert the premises into flats, and erect a further six houses on the ↵ land. It was held that in refusing to sell the hotel, in breach of contract, the vendor was liable to pay damages assessed upon the lost redevelopment potential. It can be seen that in both cases[4] the defendant *caused* the plaintiff's losses but that the defendants' state of knowledge was crucial in determining whether the court would award their full recovery. The test of remoteness, following ***Transfield Shipping Inc. v Mercator Shipping Inc., The Achilleas*** **[2008] UKHL 48, [2008] 4 All ER 159** (see also ***Siemens Building Technologies FE Ltd v Supershield Ltd*** **[2010] EWCA Civ 7, 129 Con LR 52**), may require consideration of whether a defendant has assumed responsibility for a particular loss and this may require a consideration of the commercial background to the contract.[5]

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[4] A comparison of alternative cases would suffice, eg ***Horne v Midland Railway*** **(1873) LR 8 CP 131** versus ***Simpson v L & NW Ry*** **(1876) 1 QBD 274**.

[5] The potential impact of the ***Achilleas*** on recovery of damages is briefly considered. Compare ***Attorney General of the Virgin Islands v Global Water Associates Ltd*** **[2020] UKPC 18**.

Recovery of Losses

There are four general issues which arise here: the recovery of non-pecuniary loss, the general duty imposed on the claimant to mitigate his/her losses, developments in the way loss may be calculated, and exceptional cases where damages for breach of contract may have a punitive flavour.

With regard to the first aspect, there are clear limitations on the recovery of such losses. In ***Addis v Gramophone Co. Ltd*** **[1909] AC 488**, the House of Lords stated that damages for injured feelings were generally not recoverable in a pure contract action. This prohibition was eventually questioned, with the current position being that non-pecuniary losses (eg disappointment) are recoverable provided only that *one* of the main objects of the contract is the provision of enjoyment, peace of mind, or freedom of distress, such as occurs with a standard holiday contract (eg ***Jarvis v Swan Tours Ltd*** **[1973] 1 QB 233**, ***Farley v Skinner*** **[2001] UKHL 49**). Nevertheless, these types of damages are exceptional, as illustrated by the position in most commercial contracts where even the clearest indication that the

claimant will experience anguish and vexation as a consequence of the breach will not be compensated (see ***Hayes v James and Charles Dodd* [1990] 2 All ER 815**). The limitations that are being imposed are not fully explicable by recourse to the principle of remoteness (ie the defendant could easily have been expected to contemplate such losses) but are referable to wider policy considerations. However, the more relaxed approach of the House of Lords in ***Farley v Skinner*** and the recovery of damages for mental distress in ***Hamilton Jones v David & Snape* [2003] EWHC 3147 (Ch), [2004] 1 All ER 657** have recognized further losses for which damages are recoverable.

Secondly, even if the loss which the claimant has suffered is recoverable in principle, damages will be reduced on evidence that the victim failed to mitigate his loss properly.[6] This requires the claimant

p. 194 ↵ to act reasonably in trying to minimize his/her loss and not to act unreasonably in increasing his loss. Precedent suggests that the claimant need only adopt a reasonable course of action rather than the *most* reasonable course of action. Thus, an employee who is wrongfully dismissed must take reasonable steps to find another, hopefully comparable, position. But he/she would not be expected to accept an offer of re-engagement from the original employer where his/her original dismissal occurred in particularly humiliating circumstances (compare ***Payzu v Saunders* [1919] 2 KB 581** with ***Brace v Calder* [1895] 2 QB 253**). One can justify this rule of mitigation[7] on the following grounds: either that a claimant's inaction causes the loss to occur rather than the defendant's breach, or that the defendant reasonably contemplated that the claimant would wish to minimize his/her loss rather than seek redress through the courts (but see ***White & Carter (Councils) Ltd v McGregor* [1962] AC 413**). Either way, the effect seems generally to be that the defendant should not be liable for losses which are not of his/her own making.

[6] A point is made about the duty to mitigate loss, potentially reducing the amount of damages to be awarded.

[7] Having identified and explained relevant case law, the paragraph is concluded by analysing the reasons for the duty to mitigate.

Finally, case law demonstrates that the courts are sometimes willing to devise novel mechanisms for quantifying damages or to award non-compensatory awards where the traditional methods of calculating damages might lead to injustice. For example, in ***Attorney General v Blake* [2001] 1 AC 268**[8] an account of profits was awarded against the defendant equivalent to the profits which the defendant had secured in publishing his memoirs as an ex-employee of the UK Secret Intelligence Service, in breach of his undertaking of confidentiality, even though the information no longer remained confidential. The normal rules for the award of damages suggested that the claimant had not suffered a pecuniary loss but the House of Lords held that the claimant possessed a *legitimate interest* in

preventing publication of the said memoirs for reasons of staff morale and the need to discourage revelations from other employees, the account of profits securing those twin aims. Comparable innovations can be observed in the line of cases[9] stemming from ***Wrotham Park Estate Co. Ltd v Parkside Homes Ltd*** **[1974] 2 All ER 321** where courts have been prepared to award damages based on the release of a hypothetical order for specific performance, or a hypothetically negotiated payment for the relaxation of an existing covenant within a contract (although note the curtailing of this line of authority in ***Morris-Garner v One Step (Support) Ltd*** **[2018] UKSC 20**—discussed in **Chapter 12**).

[8] Here there is a discussion of a difficult case, which does not fit neatly into the law of damages relating to compensation of loss.

[9] Other developments in this area are identified and supported by case authority.

Conclusion

In conclusion,[10] the foregoing analysis demonstrates the limits on the recovery of loss caused by the defendant's breach; that is causation, ↵ remoteness, non-pecuniary losses, and mitigation. In a commercial sense it seems fair that the defendant should not be liable for losses which he could never have contemplated. Both parties take risks when entering into a contract and part of the allocation of those risks is that non-recoverable loss might be suffered by the victim of a breach. Conversely, case law, such as ***Blake***, has demonstrated that courts are prepared, in exceptional circumstances, to bend those rules where a purposeful breach of contract leaves the claimant without any damages under traditional principles. In so doing, the law continues to reflect the ever-present tension between the layman's assumption that all losses flowing from a breach of contract should be compensated and the economist's view that a contract represents a man-made instrument of risk allocation, in which the precise reimbursement of loss for breach is often of secondary importance to the strategic commercial imperatives governing the original process of contract formation.

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[10] A conclusion draws together the points made and their relationship to the question asked.

Looking for extra marks?

■ In relation to non-pecuniary loss, the good student might also consider the difficulties of recovering damages for injured reputation. A summary of the general principle linked to a couple of exceptions might demonstrate to the examiner a useful breadth of knowledge, for example, damage to reputation and ***Anglo-Continental Holidays Ltd v Typaldos Lines (London) Ltd*** **[1967] 2 Lloyd's Rep 61**; or even damage to personal reputation and ***McLeish v Amoo-Gottfried*** **(1993) 10 PN 102**.

■ The time available for your answer will not permit you to deal with all the issues raised in great depth. Ensure that you raise all the issues relevant to the question, and that these are clearly linked to the argument in your answer.

Taking things further

■ Capper, D., 'Damages for Distress and Disappointment—Problem Solved' (2002) 118 LQR 193.

Considers the decision of the House of Lords in ***Farley v Skinner*** **[2001] UKHL 49, 2002 2 AC 732** *and its relationship with* ***Ruxley v Forsyth*** **[1996] AC 344**.

■ Chandler, A. and Devenney, J., 'Breach of Contract and the Expectation Deficit: Inconvenience and Disappointment' [2007] 27 LS 126.

Argues that development of the law justifies the award of damages for inconvenience and disappointment as compensation for lost expectation.

p. 196 ↵ ■ Coote, B., 'Contract Damages, *Ruxley* and the Performance Interest' (1997) 56 CLJ 537.

Explores the impact of the case of ***Ruxley Electronics and Construction Ltd v Forsyth*** **[1996] AC 344** *and protection of the performance interest.*

■ Hunter, H., 'Has *The Achilleas* Sunk?' (2014) 31 JCL 120.

An exploration of the rule of remoteness as stated in ***Transfield Shipping Inc. v Mercator Shipping Inc., The Achilleas*** **[2008] UKHL 48, [2008] 4 All ER 159** *in the light of subsequent case law and offers a comparison with the law in Singapore.*

■ Kramer, A., 'The New Test of Remoteness in Contract' (2009) 125 LQR 408.

Gives an analysis of the rule of remoteness as stated by the House of Lords in ***The Achilleas***.

■ McKendrick, E., 'Breach of Contract and the Meaning of Loss' [1999] 52(1) CLP 53.

Looks at the meaning of loss and argues that damages should be available for non-financial losses caused by breach of contract.

■ Summers, A., 'Unresolved issues in the law on penalties' [2017] LMCLQ 95.

Discusses ***Makdessi v Cavendish Square Holdings BV*** **[2015] UKSC 67**.