

A sailor owns a boat that she charts for sport fishing at a \$500 daily rate. The fee includes the use of the boat with the sailor as the captain, and one other crew member, as well as fishing tackle and bait. On May 1, a customer agreed with the sailor that the customer would have the full-day use of the boat on May 15 for himself and his family for \$500. The customer paid an advance deposit of \$200 and signed an agreement that the deposit could be retained by the sailor as liquidated damages in the event the customer canceled or failed to appear. At the time of contracting, the sailor told the customer to be at the dock at 5:00 a.m. on May 15. The customer and his family, however, did not show up on May 15 until noon. In the meantime, the sailor agreed at 10:00 a.m. to take a third party and her family out fishing for the rest of the day. The third party had happened to come by and inquire about the possibility of such an outing. In view of the late hour, the sailor charged the third party \$400 and stayed out two hours beyond the customary return time. The customer's failure to appear until noon was due to the fact that he had been trying to charter another boat across the bay at a lower rate and had gotten lost after he was unsuccessful in getting such a charter.

Which of the following is an accurate statement concerning the legal obligations of the parties?

- A. The sailor can retain the \$200 paid by the customer, because it would be difficult for the sailor to establish her actual damages and the sum appears to have been a reasonable forecast in light of anticipated loss of profit from the charter.
- B. The sailor is entitled to retain only \$50 (10% of the contract price) and must return \$150 to the customer.
- C. The sailor must return \$100 to the customer, because the liquidated-damage clause under the circumstances would operate as a penalty.
- D. The sailor must return \$100 to the customer in order to avoid her own unjust enrichment at the customer's expense.

Explanation:

Purpose of compensatory damages

Primary (expectation measure)	Place nonbreaching party in same position as if contract had been performed Expectation measure includes: Expectation damages Incidental damages Consequential damages
Fallback (reliance measure)	When expectation measure too speculative, place nonbreaching party in same position as if no contract had been formed Reliance measure includes: Reliance damages Liquidated damages Restitution

To recover damages, a party must prove the dollar amount of the damages with reasonable certainty. Where it would be **difficult to establish actual damages**, the parties may **agree to liquidated damages**—ie, a fixed measure of damages for breach set forth in the contract. However, a liquidated-damages clause is **unenforceable** as a **penalty** if the amount is so **unreasonably large in relation to actual or anticipated damages** that it punishes the breaching party (as opposed to merely compensating the nonbreaching party).

Here, the customer contracted to use the sailor's boat for a full day for \$500. The customer paid a \$200 deposit, which the sailor could retain as liquidated damages if the customer canceled or failed to appear. Although the sailor ultimately collected \$600 for the day (\$200 retained deposit + \$400 from the third party), she also stayed out two hours later than the customary return time as a result of the customer's breach. As a result, the \$200 appears to have been a reasonable measure of damages, and the sailor can retain the full amount **(Choice C)**.

(Choice B) There is no rule that, if applied, would result in the sailor retaining \$50 (10% of the contract price).

(Choice D) **Restitutionary damages** ensure that the nonbreaching party (here, the sailor) is not unjustly enriched—ie, does not receive a benefit that was not rightfully earned and would be unfair to keep. But here, the parties agreed to the deposit as a reasonable amount of damages in the event of the customer's breach.

Educational objective:

A liquidated-damages clause is unenforceable as a penalty if the amount is so unreasonably large in relation to actual or anticipated damages that it punishes the nonbreaching party.

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