DAMAGES, PART 2
Agreed Damages

- Liquidated Damages

Generally, contracts that involve the exchange of money or the promise of performance have a liquidated damages stipulation. The purpose of this stipulation is to establish a predetermined sum that must be paid if a party fails to perform as promised.

Damages can be liquidated in a contract only if
- (1) the damages are intended to function as damages, not as a penalty;
- (2) the injury is either "uncertain" or "difficult to quantify";
- (3) the amount is reasonable and considers the actual or anticipated harm caused by the contract breach, the difficulty of proving the loss, and the difficulty of finding another, adequate remedy.

If these criteria are not met, a liquidated damages clause will be void.
(1) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.

Bolded language in UCC but not Restatement 2d
Liquidated Damages and Penalties

- Strong general rule - Courts will not enforce penalty clauses (provisions in a contract that stipulate an excessive pecuniary charge against a defaulting party).

- Penalty is designed to prevent a party from breaching (and may, therefore, not encourage economic efficiency).

- Liquidated damages are designed to promote economic efficiency by establishing reasonable damages and avoiding the need for a third party to set them.
Intention

- While part of the traditional definition, courts give intention (or at least stated intention) of the parties little weight in determining whether a clause is a penalty liquidated damages. The labeling of the provision is not determinative.

- Neither UCC nor Restatement 2d considers intention a relevant line of inquiry.
Injury Uncertain or Difficult to Quantify

- If damages are not uncertain, there is no need to liquidate them.

- UCC and Restatement speak not of “uncertainty” but of “the difficulties of proof of loss.”
Reasonableness

- Liquidated damages clause with unreasonably high “damages” = penalty clause. Unreasonably low “damages” are not a penalty, but may be struck down as unconscionable.

- Traditional rule - reasonableness judged as of the time of agreement

- Modern rule (UCC) - “reasonable in the light of the anticipated or actual harm caused by the breach.” It is an either or test, and must be reasonable at one of the two times.
Liquidated Damages

- If amount is a reasonable estimate at the time of contracting, but no actual damage arises, authorities are split on whether to enforce Liquidated Damages clause.

- Liquidated damages can be expressed as a formula rather than a sum certain.
Two Pitfalls of Draftsmanship

- A liquidated damages clause that provides the same “damages” for all breaches, big and small, is not a reasonable pre-estimate of losses.

- Clauses that provide for liquidated damages but also allow suit for additional actual damages have generally been struck down.

- Liquidated Damages and Specific Performance

- The two remedies are separate and obtaining liquidated damages does not cut off rights to Specific Performance (Law vs. Equity distinction).
Efficient Breach Theory

Should "Efficient Breaches" Be Encouraged?

- What constitutes true efficiency?
- Opportunity costs
- Non-monetary costs
- Trust
Restitution as a Remedy For Breach
Restitution as a Remedy For Breach

- Meaning of Restitution: Unjust Enrichment

- Encompasses recovery of money judgment in quasi contract action as well as equitable remedies for specific relief such as decrees that cancel deeds, or impose constructive trusts or equitable liens.

- “A person who has been unjustly enriched at the expense of another is required to make restitution to the other.” Restatement 1st Restitution, pg. 1.

- Unjust enrichment vs. unjust impoverishment
Restitution as an Alternative Remedy for Breach

- Remedy only for total, not partial, breach

- Seeking restitution implicitly requires electing to cancel the contract.
Measure of Recovery

- Basic aim of restitution is to put party back in pre-contracting position.

- Recovery (other than specific restitution) is for goods delivered, services rendered, or property conveyed, less the reasonable value of any counter performance received.

- Does not involve unjust enrichment.
Restitution

- Traditional rule - acts that are merely preparatory to performance do not justify action for restitution.

- Modern rule - more lenient on what may be recovered - reliance damages.
Specific Restitution

- Same rules apply as in Specific Performance, plus, traditionally, plaintiff must show the inadequacy of the legal remedy (damages). Restatement 2d urges dropping the additional requirement, but no supporting authority yet.

- Factors of inadequacy - Uniqueness (not as routine as with Specific Performance), speculative nature of damages, and judgment-proof nature of defendant.

- Sale of property at issue to a third party for bona fide value cuts off specific restitution.
Recovery of Both Damages and Restitution

- Plaintiff must, at some point, choose between damages and restitution.

(1) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2-612), the buyer may cancel and whether or not he has done so may, in addition to recovering so much of the price as has been paid,

(a) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or

(b) recover damages for non-delivery as provided in this Article (Section 2-713).