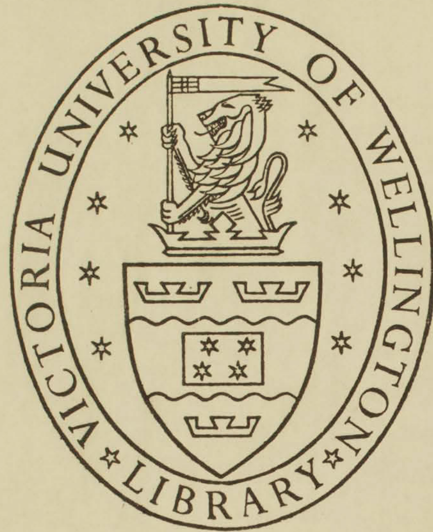
LX Fr FRENCH, M.P. Damages for pre-contract expenditure

LX Fr

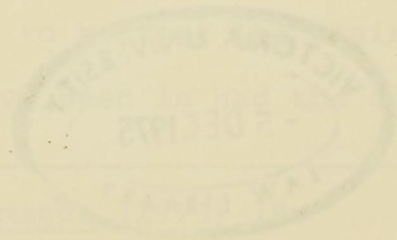

VICTORIA UNIVERSITY OF WELLINGTON
LIBRARY

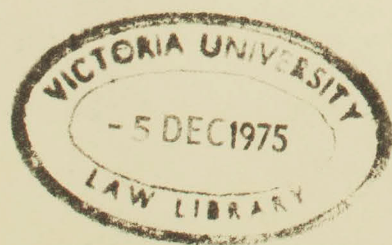
MICHAEL PAUL FRENCH

"DAMAGES FOR PRE-CONTRACT EXPENDITURE"

Submitted for the LL.B. (Honours) Degree
at the Victoria University of Wellington.

1 September, 1975.




VICTORIA UNIVERSITY
- 5 DEC 1975
LAW LIBRARY

333,988

L
Folder
FRENCH, M.P.

I. INTRODUCTION

It is well established that in awarding damages for breach of contract the normal measure should be the expectancy interest or loss of anticipated profits.[1] The measure seeks to put the plaintiff in the same position as if the contract had been performed. Nevertheless, it is recognised that this measure of damages may not be a satisfactory remedy in all instances. The facts of McRae v Commonwealth Disposals Commission[2] are well known. The plaintiff purported to sell to the plaintiff the wreck of an oil tanker. The plaintiff fitted out an expedition to salvage the wreck but found that there was not and never had been any such tanker. The plaintiff claimed his expectancy interest but the High Court of Australia held that there was insufficient evidence of the value of the tanker. However to deny recovery entirely would obviously have been unfair and the court held that the plaintiff could recover the expenses incurred in mounting the salvage expedition.

The basis of recovery in that case was the reliance interest[3] award which is based on the doctrine of restitutio in integrum - the tort measure of damages. The measure attempts to restore the plaintiff to the position he would have been in had the contract not been

[1] Ogus, The Law of Damages (1973) 18.
[2] (1951) 84 C.L.R. 377.
[3] Ogus, ante n.1, 17.

Victoria University of Wellington Law Library

FR FRENCH, M.P. Damages for Pre-contract expenditure

L.C

L
Folder | FRENCH, M.P.

made by allowing him to recover expenditure rendered futile as a result of the breach. Although this measure of damages is usually only claimed where it is impossible to calculate the expectancy interest award with any certainty,it is now accepted that the reliance interest award is a true alternative to the expectancy interest award and the plaintiff has a right to elect between the two measures.[4]

How far can alternative measures of contract damages be applied? When parties enter into a contract it gives rise to legally enforceable obligations which bind them to it. In performing these obligations it may be necessary to incur certain expenditure and, in the majority of cases, a person will wait until he has entered into the contract before he commits himself to this, simply because if no contact eventuates he will have to bear the loss of this expenditure himself. In some instances however, he may be willing to accept that risk because, in order for the proposed objects to be achieved, it is essential that certain commitments be made immediately irrespective of whether the contract is in existence or not. Such expenditure will usually only be made where, on a consideration of all the factors, it is apparent that

---

[4] See eg., Anglia Television Ltd v Reed [1972] 1 Q.B. 60, 63-64. Cullinane v British 'Rema' Manufacturing Co Ltd [1954] 1 Q.B. 292, 303.

FRENCH, M.P. Damages for Pre-contract expenditure

L
Folder
FRENCH, M.P.

the advantages of committing the expenditure now, and perhaps having to forfeit it if no contract is entered into, outweigh the advantages to be gained from waiting for the contract to be executed before committing it.

Expenditure incurred in anticipation of entering into the contract will be substantially the same as the expenditure which would have to be incurred if the contract was in existence. Once the parties have entered into the contract therefore, the fact that the expenditure is pre-contract will have little practical effect on them. The expenditure may have influenced the contract 'price' but the parties, having agreed upon the terms of the contract, would have entered into it with 'their eyes open.'

The issue under discussion in this paper arises in the situation where the defendant has breached the contract and the plaintiff's pre-contract expenditure is rendered useless as a result of that breach. The question is whether, in an action for breach of contract, the plaintiff can recover this loss of pre-contract expenditure. Suppose, for example, that the plaintiff's expenditure in <u>McRae</u> v <u>Commonwealth Disposals Commission</u> had been incurred before the contract with the defendant had been entered into. Would the court still have allowed the recovery of that expenditure. In 1972 the

FRENCH, M.P. Damages for pre-contract expenditure

L Folder FRENCH, M.P.

English Court of Appeal in Anglia Television Ltd v Reed[5] held that the plaintiff company could recover its wasted expenditure even though it had been incurred before the contract with the defendant had been entered into. Prior to this decision the position of the English jurisdiction on the issue of the recovery of pre-contract expenditure had been very uncertain. The American position, on the other hand, appears to be well settled and, except in a few instances where special fact situations exist, the recovery of pre-contract expenditure is not permitted. The issue has been raised in two recent New Zealand cases[6] but the court did not attempt to resolve it and the question is still open.

The different decisions reached in cases raising the issue have resulted to a large degree from the varying application to this specific area of the general principles relating to contract damages. In this paper it is proposed to set out the approach of both the English and American courts in dealing with the issue and, in particular, to examine the treatment of these general principles. The effect of the decision in Anglia T.V. v Reed will be considered. Then, in the light of this examination, it will be suggested that the recovery of pre-contract expenditure should be permitted in an action for breach of contract.

---

5 [1972] 1 Q.B. 60; hereinafter referred to as Anglia T.V. v Reed.

6 Ash v Victor Enterprises Ltd (unreported) Cooke J. in the Supreme Court of New Zealand, August 5 1974; (A. 591/70).
Moola Bar v Brierley-Jones Investments (N.Z.) Ltd (unreported) Cooke J. in the Supreme Court of New Zealand, March 18 1975; (A. 18/72)

Fr FRENCH, M.P. Damages for Pre-contract expenditure

L.C

L Folder FRENCH, M.P.

II THE ENGLISH POSITION - Pre Anglia T.V. v Reed

Because it is only in exceptional circumstances that expenditure will be incurred before there is a contractual basis for it, the issue of the recovery of pre-contract expenditure has made few appearances in the case law. The earliest consideration of the question appears to have been in the case Hodges v Earl of Litchfield[7] where the vendor was unable to complete a contract for the sale of an estate because of an inability to make out a title. It was held that the purchaser could not recover as damages expenses incurred prior to entry into the contract. Tindal C.J. said:[8]

> The expenses preliminary to the contract ought not to be allowed. The party enters into them for his own benefit, at a time when it is uncertain whether there will be any contract or not.

Over a hundred years later in Perestrello e Companhia Limitada v United Paint Co. Ltd[9] the plaintiff company claimed damages from the defendant for breach of a contract which purported to give the plaintiff exclusive rights to manufacture and distribute a

---

[7] (1835) 1 Bing. N.C. 492; 131 E.R. 1207.

[8] Ibid., 498

[9] The Times, April 16, 1969 (1969) 113 S.J. 324.

In the lower court the plaintiff had claimed for his loss of expenditure but then attempted to amend the statement of claim to add a claim for loss of profits. The lower court judge found that the plaintiff was not entitled to claim for loss of profits on the pleadings as they stood, refused leave to amend and adjourned the case generally.

The plaintiff appealed on the ground that the judge had erred in refusing leave to amend and that notwithstanding that refusal they were entitled to lead evidence in support of their claim for loss of profits. It is this appeal which appears in the official reports (cf. [1969] 1 W.L.R. 570).

FRENCH, M.P. Damages for pre-contract expenditure

L
Folder
FRENCH, M.P.

particular paint product in Portugal. The damages claimed represented expenditure incurred prior to, and in anticipation of, the making of the contract - the largest items being the cost of adaptation of a factory building, the provision of special containers and the printing and distribution of advertising material. Thesiger J., supporting the decision in Hodges v Earl of Litchfield, held that the recovery of pre-contract expenditure would be consistent neither with the expectancy interest award nor the reliance interest award and that, therefore, there was no basis for such recovery. His Lordship also said that the rule in Hadley v Baxendale,[10] which based recovery on whether, at the time the contract was made, the loss was reasonably forseeable as likely to result from the breach, could not be relied upon to support the plaintiff's claim since it assumed that the loss arose after, and resulted from, the breach and this could not be said of the wasted pre-contract expenditure.

There was, however, a long established rule in England that where the vendor of land fails to complete by reason of a defect in his title, the purchaser cannot claim damages for loss of his bargain but must restrict his damages claim to a recovery of the money he has laid out.[11] Usually this amounted to a recovery

---

[10] (1854) 9 Exch. 341; 155 E.R. 145.

[11] Flureau v Thornhill (1776) 2 Wm. Bl. 1078; 96 E.R. 635. Bain v Fothergill (1874) L.R. 7 H.L. 158.

FRENCH, M.P. Damages for Pre-contract expenditure

L
Folder
FRENCH, M.P.

of the deposit paid and the expenses of investigating the title but in Hanslip v Padwick,[12] where the vendor failed to complete but not through a defect in title, it was held that the purchaser could also recover any expenses incurred in executing the contract. The situation here is distinguishable from that in Hodges v Earl of Litchfield where the damages claimed were for monies paid by the plaintiff to his agent which did not represent such costs.

In Wallington v Townsend[13] the vendor in a contract for the sale of land refused to convey the property even though he was capable of doing so. The court held that the plaintiff was entitled to recover the conveyancing expenses to which she had been put, including the legal costs incurred prior to the execution of the contract and also interest, by way of damages for breach of contract from the date when the deposit was lodged and not merely from the date of the contract. The court, per Morton J., said:[14]

> I think the true view is that in a case where the vendor under a contract for the sale of land has refused to carry out the contract, and the failure to carry out the contract is not due to a defect in the vendor's title, the damages are at large and the Court can give such damages as, according to general principles, it thinks right.

12 (1850) 5 Exch. 615; 155 E.R. 269.

13 [1939] Ch. 588.

14 Ibid., 592-193.

X Fr FRENCH, M.P. Damages for Pre-contract expenditure

Folder FRENCH, M.P.

A similar situation arose in Lloyd v Stanbury[15]. The defendant had agreed to sell a plot of land to the plaintiff and contracts were exchanged and signed but the defendant refused to complete on the ground that one parcel of land had been mistakenly included in the contract. Brightman J. in considering the dicta of Morton J. in Wallington v Townsend said:[16]

> It appears to me that the decision is at least some authority that a disappointed buyer suing for damages because the vendor is not willing to implement the bargain is not limited to compensation for expenditure incurred strictly after the execution of the contract. In my judgement the damages which he is entitled to recover include expenditure incurred prior to the contract representing (1) legal costs of approving and executing the contract and (2) the costs of performing an act required to be done by the contract notwithstanding that the act is performed in anticipation of the execution of the contract. In addition the buyer is entitled on general principles to damages for any other loss which ought to be regarded as within the contemplation of the parties.

On the basis of this observation Brightman J. permitted the plaintiff to recover his expense in moving a caravan and furniture to the site, even though this expense had been incurred in anticipation of the contract and before it was concluded, because it was "within the contemplation of the parties when the contract was signed."[17]

At this stage the English position on the issue was rather uncertain with different approaches being taken by the courts. It has been suggested that the Wallington v

---

[15] [1971] 1 W.L.R. 535.

[16] Ibid., 546.

[17] Ibid., 547.

FR FRENCH, M.P. Damages for Pre-contract expenditure

L.C

Folder FRENCH, M.P.

Townsend and Lloyd v Stanbury type of situation could be distinguished from the other cases on the ground that they were dealing with transactions concerning the sale of land.[18] This distinction is not very convincing however when it is considered how far the principles were extended in the granting of damages. Allowing recovery of the expenditure incurred in the moving of the caravan and furniture in Lloyd v Stanbury, for example, can hardly be said to be justified purely on the ground that the transaction was one concerning the sale of land.

Ogus,[19] while denying the right to recover pre-contract expenditure generally, concedes that where there has been a substantial agreement between the parties it would be unfair to disallow a claim for expense which had been incurred at this stage. It is, however, difficult to reconcile this statement with the grounds on which the recovery is denied in other circumstances. The expenditure is still incurred before the contract is entered into and, as the American cases indicate,[20] it would be drawing rather a fine distinction to say that there is any greater causal connection between the loss and the breach just because there has been a substantial agreement. Certainly, the recovery of this expenditure is no more able to be accommodated under the expectancy or reliance interests than if there had been no agreement at all.

---

18 McGregor, The Law of Damages (13th ed. 1972) 34.
19 Ante, n.1, 350.
20 Post, n. 34.

FRENCH, M.P. Damages for Pre-contract expenditure

L.C

Folder FRENCH, M.P.

In any event, this was the state of the law when, in 1972, the Anglia T.V. v Reed case came before the English Court of Appeal.

III THE AMERICAN POSITION

In America the rule which has emerged is that the defendant is not liable for expenditure incurred before the actual making of the contract unless he is shown to have assumed responsibility for it.[21] This rule applies even if the expenditure was incurred directly for the purpose for which the plaintiff made the contract.

In Hough v Jay-Dee Realty and Investment Inc.[22] there was an action for breach of the defendant's convenant to construct and deliver possession of a restaurant building to the plaintiff. Amongst other damage claims, the plaintiff claimed for pre-contract expenditure rendered useless as a result of the breach. Believing it necessary, and anticipating the commencement of his new business, the plaintiff had closed the restaurant he was running at the time of the preliminary negotiations and began devoting his full time to the preparation necessary for the establishment and operation of the new business before the execution of the agreement. The court held that the recovery of certain expenses and out-of-pocket loss incurred after the agreement was executed was allowable but that expenses incurred before

---

21 Curran v Smith C.A. 3d. Pa.; 149F. 245 (1906).

22 401 S.W. 2d. 545 (1966).

FRENCH, M.P. Damages for Pre-contract expenditure

Folder FRENCH, M.P.

the contract was entered into were not recoverable:[23]

> Plaintiffs' expenditures during that period were not referable to the contract or its breach. Expenses incurred during preliminary negotiation are not usually recoverable in an action for breach of contract .... and in this case they were incurred before any enforceable obligation arose....

Even where there has been a substantial agreement as to the contract and its contents, pre-contract expenditure will not be recoverable. In Chicago Coliseum Club v Dempsey[24] the plaintiff sought damages for breach of a contract for a championship boxing match. The court held that although the profits were not susceptible of legal determination, the plaintiff could not recover its expenditure incurred prior to the actual execution of the contract. This was held even though the negotiations between the parties had clearly indicated an agreement between them and the contract was dated a week previous to its actual execution and the expenditure incurred after the date inserted.

There are numerous other cases to the same effect. The plaintiff's time and expense in making journeys to secure the contract cannot be recovered.[25] Without some express agreement to that effect, one who sells his business at a loss, journeys to the location of a prospective employer, and remains there during negotiations for a contract, cannot recover these losses upon the employer's

---

23 Ibid., 551.

24 265 ILL. App. 542 (1932).

25 Stevens v Lyford 7 N.H. 360 (1834).

FRENCH, M.P. Damages for pre-contract expenditure

Folder FRENCH, M.P.

breach of a resulting contract to employ.[26] The time spent by the plaintiff in negotiating or making the contract is not an item of damages for breach.[27] The expense of a seller's representative in travelling to the buyer's place of business to sell his goods is not recoverable in an action by the seller for refusing delivery.[28] And, similarly, the plaintiff cannot recover a commission paid or promised to a broker for securing the contract.[29]

There have been instances in the American case law where the recovery of pre-contract expenditure has been allowed but these cases have been decided on the particular fact situations involved. In Security Stove and Manufacturing Co. v American Railway Express Co.[30] the plaintiff manufactured equipment which it desired to exhibit at a convention. Because time was of the essence the plaintiff engaged space for the exhibit and then arranged for the defendants to deliver the equipment. The defendant was made fully aware of the circumstances and the date upon which delivery was necessary. The defendant failed to deliver a vital part of the apparatus and consequently it was unable to be exhibited. The court held the defendant liable, in addition to the costs of the carriage, for the amount paid by the plaintiff

---

26 Marsh v South Atlantic Casket Co. 29 Ga. App. 394; 115 S.E. 502 (1923).

27 Durkee v Mott 8 Barb. 423 (1850 N.Y.).

28 Halliday v Lesh 85 Mo. App. 285 (1900).

29 Linde v Ellis 224 Ky. 649; 6 S.W. 2d. 1089 (1928). Manning v Pounds 2 Conn. Cir. 344; 199A. 2d. 188 (1963).

30 227 Mo. App. 175; 51 S.W. 2d. 572 (1932).

Fr FRENCH, M.P. Damages for Pre-contract expenditure

L.C

Folder FRENCH, M.P.

to rent the space. The court said:[31]

> While it is true that the plaintiff already had incurred some of these expenses, in that it had rented space at the exhibit before entering into the contract with the defendant for the shipment of the exhibit and this part of the plaintiff's damages, in a sense, arose out of a circumstance which transpired before the contract was even entered into, yet, plaintiff arranged for the exhibit knowing that it could call upon the defendant to perform its common law duty to accept and transport the shipment with reasonable dispatch.

Thus the plaintiff was allowed to recover his pre-contract expenditure in this case because the defendant was under an obligation at common law to perform the contract when called upon to do so.[32] The situation was substantially the same as if the contract had been in existence when the expenditure was incurred. The courts have regarded cases such as this[33] as being outside the scope of the rule altogether rather than as true exceptions to the rule and the indications are that they will only be invoked as authority for cases with similar fact situations.

As in the English cases of Hodges v Earl of Litchfield and Perestrello e Companhia Ltda. v United Paint Co. Ltd, the American position is that the pre-contract expenditure is not recoverable in an action for breach of contract. The rationale behind this conclusion is that an action for damages can only include losses sustained as a consequence of the contract and since pre-contract expenditure is not incurred in preparation and part performance it cannot be

[31] Ibid., 577.

[32] For the situation as regards the duties of the common carrier see, Garrow and Gray, Law of Personal Property in New Zealand (5th ed. 1968) 92. The situation here is similar to that in the United States.

[33] See eg. Goodman v Dicker 83 App. D.C. 353; 169F. 2d.684 (1948).

Fr FRENCH, M.P. Damages for Pre-contract expenditure

L
Folder
Fr
FRENCH, M.P.

said that their loss was caused either by the breach of the contract or its making.[34]

IV ANGLIA TELEVISION LTD v REED[35]

In 1972 the English Court of Appeal was required to consider whether there could be recovery of pre-contract expenditure in an action for breach of contract. In Anglia T.V. v Reed the plaintiffs, a television company, entered into negotiations with the defendant, a well known screen actor, for him to act the leading role in a play which they were planning to produce for television. The contract was finally signed but the defendant discovered that there had been some misunderstanding over his bookings and he was forced to repudiate the contract. The plaintiffs could not find a suitable replacement and abandoned the proposed production.

The plaintiffs sued the defendant for breach but were not able to quantify with any certainty what loss of anticipated profits they had suffered as a result of the breach. Instead they claimed their total wasted expenditure, most of which had been incurred before the contract with the defendant had been entered into. This pre-contract expenditure included such items as the costs involved in arranging a location and engaging certain key personnel such as a director, a designer and a stage manager.

---

[34] Corbin, The Law of Contracts (1964) v. 207.

[35] [1972] 1 Q.B 60.

Fr FRENCH, M.P. Damages for Pre-contract expenditure
L.C

L
Folder
Fr
FRENCH, M.P.
Damages for...

The defendant did not dispute his liability but he argued that he was only liable for the damages incurred after the contract was concluded and not those incurred before. The lower court rejected this contention and held that the plaintiff could recover the total damages claimed. This decision was upheld on appeal. In the Court of Appeal Lord Denning M.R. delivered the judgment of the court with the concurrence of Phillimore and Megaw L.J.J.

Denning M.R. said regarding the recovery of pre-contract expenditure, that he could not "accept the proposition as stated" in the decisions of Hodges v Earl of Litchfield and Perestrello e Companhia Ltda. v United Paint Co. Ltd.[36] In an action for breach of contract, according to Denning M.R., the plaintiff may elect between claiming his loss of profits or his wasted expenditure.[37] If he chooses to claim his wasted expenditure, however, he is not restricted to a recovery of the post-contract expenditure but can also claim for expenditure incurred before the contract is entered into "provided that it was such as would reasonably be in the contemplation of the parties as likely to be wasted if the contract was broken."[38] On the facts of the case, Denning M.R. found that the defendant probably knew that certain expenditure had already been incurred at the time

[36] Ibid., 63.
[37] Ibid., 63-64.
[38] Ibid., 64.

Fr FRENCH, M.P. Damages for Pre-contract expenditure
L.C

L
Folder
Fr

FRENCH, M.P.
Damages for pre-

the contract was made and consequently[39]

> He must have contemplated - or, at any rate, it is reasonably to be imputed to him - that if he broke his contract, all that expenditure would be wasted, whether or not it was incurred before or after the contract.

His Lordship applied the forseeability principle, first laid down in Hadley v Baxendale,[40] to determine whether the pre-contract expenditure was recoverable and found support for this approach in the judgement of Brightman J. in Lloyd v Stanbury.[41]

The appeal was dismissed on this ground but in reaching his decision, Denning M.R. accepted without question the idea that pre-contract expenditure could be wasted as a result of the defendant's breach of contract. Once such a breach had occurred, Denning M.R. concluded, the defendant could not deny his liability for any losses resulting from that breach.[42]

It has been suggested that the case of Anglia T.V. v Reed can be distinguished from the case of Hodges v Earl of Litchfield on the ground that in the latter case the claim was for the money that the plaintiff had paid to his experts while in the former it was a claim for the loss of profits which the plaintiff would have earned if the defendant had not broken his contract.[43] But this

---

39 Idem.
40 Post n. 58.
41 Supra n. 16.
42 [1972] 1 Q.B. 60, 64.
43 (1972) 88 L.Q.R. 169.

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

L
Folder
Fr

FRENCH, M.P.
Damages for pre-

distinction, if valid, would still fail to reconcile the different approaches taken in the two cases. Tindal C.J. in Hodges v Earl of Litchfield denied the right to recover any pre-contract expenditure at all and this position was supported by Thesiger J. in Perestrello e Companhia Ltda. v United Paint Co Ltd. In neither case was the recovery denied by reference to any fact other than that the expenditure had been incurred before the contract was entered into.

Denning M.R. in Anglia T.V. v Reed, while not denying that in some cases the recovery of pre-contract expenditure should not be allowed, held that such recovery should be permitted subject to the general principles which govern the recovery of the more common heads of contract damages.

In accepting that there was a causal connection between the wasted pre-contract expenditure and the defendant's breach of contract, Denning M.R. brought the English position into a direct conflict with the American position. There is, however, unlikely to be any reaction to this decision from the American jurisdiction. In view of the controversy surrounding the issue, it is perhaps unfortunate that Denning M.R. did not go to greater length to explain the reasoning behind his decision. Nevertheless, in this writer's opinion and for the reasons which it is now proposed to examine the decision reached in Anglia T.V. v Reed was correct.

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

L
Folder
Fr

FRENCH, M.P.
Damages for pre-

V PRE-CONTRACT EXPENDITURE and the EXPECTANCY and RELIANCE INTERESTS

One of the grounds on which Thesiger J. in Perestrello e Companhia Ltda. v United Paint Co. Ltd denied recovery of pre-contract expenditure was that such recovery would be consistent with neither the expectancy nor the reliance interest awards.[44] It is doubtful whether this reasoning is sound.

Expenditure incurred prior to entry into a contract cannot be incurred in reliance upon that contract since, at the time the expenditure is incurred, it is not yet in existence. At the point of time immediately before the contract is entered into (that is, the time at which the reliance interest award seeks to place the plaintiff) any pre-contract expenditure would, by definition, have already been made. To allow the recovery of this expenditure, therefore, would put the plaintiff in a better position than he would have occupied had the contract not been made[45] and this would be inconsistent with the very essence of the reliance interest award.

The expectancy interest, on the other hand, seeks to place the plaintiff in as good a position as he would have occupied had the contract been performed. The

---

[44] Supra, n. 9.

[45] Ogus, "Damages for Pre-Contract Expenditure" (1972) 35 M.L.R. 423, 424-425.

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

L
Folder
Fr
FRENCH, M.P.
Damages for pre-

recovery of pre-contract expenditure bears no relation to such an award but it has been suggested that, where the expectancy interest is claimed, any pre-contract expenditure incurred may be taken into account in calculating the profit which would have been made had the contract been performed.[46] In the calculation of lost profits, an allowance is made for expenses necessarily incurred and it would seem unreasonable to exclude expenses which related to the profitable transaction but which were incurred before the contract was entered into. If such expenses were to be taken into account when calculating the expectancy interest award however, it would be anomalous to deny an alternative claim for damages based on the wasted pre-contract expenditure. To do so would be to fully compensate the plaintiff who was in the fortunate position of being able to prove his lost profits but to deny recovery entirely to the plaintiff who was unable to do so.

Pre-contract expenditure should be taken into consideration in awarding damages where the promised performance is of such a nature that the defendant's breach makes it impossible to calculate the value of the expectancy interest. A similar approach was taken by the court in McRae v Commonwealth Disposals Commission[47] in awarding the reliance interest. The High Court of

---

[46] Ibid., 426.

[47] Supra, n. 2.

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

Folder Fr FRENCH, M.P. Damages for pre-

Australia held that the defendant had impliedly undertaken that there was a tanker and that for the breach of this undertaking it was to pay damages amounting to the cost of the salvage operation plus the amount paid by the plaintiff to the defendant for the alleged tanker. The defendant argued that the plaintiff could not recover for expenses rendered futile because he was not in a position to show that there was any profit to be had in finding the tanker. This argument was rejected on the ground that it was, in this case, the defendant's own breach of contract that made it impossible to show whether or not the plaintiff could have made any profit.

The reluctance by some academic writers[48] to allow the recovery of pre-contract expenditure in all situations has stemmed in part from a problem which relates to the recovery of expenditure generally. Where it can be shown that the plaintiff had made a 'bad bargain' - he would have made a loss on the contract had it been performed - it would put the plaintiff in a better position than if the contract had been performed if the recovery of all expenditure was allowed. The problem is unresolved in the case law but the view favoured by academic opinion is that in such a situation the expectancy interest should set the limit of recovery.[49] For the purposes of this paper it is enough to recognise the issues involved and to point out that if a

[48] See eg., Ogus, ante, n. 45, 424. and (1973) 31 U.T. Fac. L.R. 139, 141-142.

[49] Ogus, ante, n. 1, 351.

FRENCH, M.P. Damages for pre-contract expenditure

L
Folder
Fr
FRENCH, M.P.
Damages for pre-

Fr
FRENCH, M.P. Damages for Pre-contract expenditure

satisfactory answer is accepted by the courts, there is no reason why it should not apply to situations involving pre-contract expenditure as well as those involving post-contract expenditure.

In any event, a claim for wasted pre-contract expenditure will usually only arise in cases where it is impossible to predict with accuracy just what profit, if any, the plaintiff would have earned had the contract been performed. It is well established however that mere difficulty of proof alone is no bar to an award of damages.[50] What can be assumed, on a prima facie basis, is that where the plaintiff has incurred expenditure prior to entering into a contract, he has done so in the belief that the profits to be accrued from the contract when it was performed would at least cover the initial outlay.[51] Therefore, it is possible to argue that preliminary expenditure can be returned to the plaintiff, not as expenditure but as an estimate of the profit he would have earned had the contract been performed.

There is some authority for this proposition. In <u>Aldwell v Bundey</u>[52] an advertisement publicised a boat race at which the first prize was to be £150. Acting on this, the plaintiff procured a boat and incurred some

---

[50] See eg., <u>Chaplin v Hicks</u> [1911] 2 K.B. 786.
[51] Ante, n. 43.
[52] (1876) S.A.S.R. 118.

L.C

L
Folder
Fr
FRENCH, M.P.
Damages for pre-

expenditure in preparing for the event. The promised race failed to materialise and a claim was made for the initial outlay. The Supreme Court of South Australia, per Stow J., pointed to the acute difficulty in this case of estimating the extent of the plaintiff's loss (that is, the chance of winning £150) and decided that there was only one method by which it could be done and that was to have regard to the preliminary expenditure: "A consideration of those expenses was the only means of estimating the plaintiff's loss."[53]

In the earlier case of Herring v Tomlin[54] the defendant declined to pursue a partnership agreement after the plaintiff had expended considerable sums both in preparation and in endeavouring to obtain employment for the partnership. The court held that although the plaintiff was not entitled to all the money he had laid out, he was nevertheless entitled to the profits he would have derived had the contract been performed. On this basis the expenses in question were recoverable, not as though they had all been lost but as showing the value of the contract broken.

McGregor[55] attempts to justify this approach by presenting the recovery of pre-contract expenditure as a 'half-way house' between the expectancy and the reliance interests: it "should be regarded as in effect giving

---

53 Ibid., 134.
54 (1854) L.T.O.S. 92.
55 Ante, n. 18, 43.

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

L
Folder
Fr
FRENCH, M.P.
Damages for pre-

the plaintiff his potential loss of profits up to the limit of his pre-contract expenditure."[56]

Even if the recovery of pre-contract expenditure cannot be explained in this way, it would be incorrect to deny the recovery merely on the grounds that it did not have a basis under the existing heads of contract damages. The principle purpose of the law of damages is compensation and,

> It is . . . clear that the things which the law of damages purports to "measure" and "determine" - the "injuries", "items of damage", "causal connections", etc. - are in considerable part its own creations, and that the process of "measuring" and "determining" them is really a part of the process of creating them.[57]

Different heads of contract damages have developed to protect the various purposes and interests of the individual, the business world and society in general. But this classification has only developed as a guideline for the courts to refer to when determining a damages claim, and was not intended to apply as a closed class to the exclusion of alternative heads of damages, which may develop to accommodate other purposes and interests. It is now proposed to consider whether pre-contract expenditure could be claimed as a separate head of contract damages.

---

56 Idem.

57 Fuller and Perdue, "The Reliance Interest in Contract Damages" (1936) 46 Yale L.J. 52.

Victoria University of
Wellington
Law Library

FRENCH, M.P. Damages for pre-contract expenditure

Folder Fr FRENCH, M.P. Damages for pre-

Fr FRENCH, M.P. Damages for Pre-contract expenditure

VI PRE-CONTRACT EXPENDITURES AND THE DOCTRINES OF FORSEEABILITY AND CAUSATION: The American Position Denied.

In Hadley v Baxendale the court considered the extent to which a plaintiff is entitled to demand damages for breach of contract. This case put forward the proposition that it is not always wise to make the defaulting promisor pay for all the damage which follows as a consequence of his breach. The proper test for determining whether particular items of damage should be recoverable is to inquire whether they should have been forseen by the promisor at the time the contract was entered into.[58] Although later cases[59] have attempted to modify this rule to some extent the basic principle remains the same and it is well accepted that the rule must be applied at the time the contract is made.[60]

Is it possible for this rule to be applied to determine whether particular items of pre-contract expenditure should be recoverable in an action for breach of contract? Hadley v Baxendale refers to losses generally and does not purport to restrict recovery to post-contract expenditures. If the recovery of a certain item of expenditure depends on whether the defendant forsaw or contemplated at the time the

---

58 (1854) 9 Exch. 341, 354; 156 E.R. 145, 151.

59 See particularly, Koufos v C. Czarnikow [1969] 1 A.C. 350 where the test was held to be the "contemplation" of the parties.

60 See eg., Victoria Laundry (Windsor) Ltd. v Newman Industries Ltd. [1949] 2 K.B. 528, 533.

Koufos v C. Czarnikow supra, n. 59, 383.

Folder Fr FRENCH, M.P.

contract was made that such damage was likely to result in the event of his breach then there is no logical reason why the recovery of pre-contract expenditure should not be determined by the same criterion.

Denning M.R. in Anglia T.V. v Reed[61] and Brightman J. in Lloyd v Stanbury[62] agreed that if the defendant at the time the contract was made understood or should have understood that he would be liable to recompense the plaintiff for a particular item of expenditure if it was rendered useless as a result of his breach, it should not matter that the expenditure had been incurred before the contract was entered into. Also, although the opposite was argued by the defendant's counsel in Anglia T.V. v Reed[63] it is suggested that the 'hypothetical reasonable man' would say at the time of the contract was made that he would be liable in the event of his breach for particular items of expenditure rendered useless as a result of that breach irrespective of whether that expenditure was incurred before or after the contract was entered into.

There is however another aspect to this question of recovery because, although it is well settled law that recovery depends on foreseeability or contemplation,

---

[61] Supra, n. 16.
[62] Supra, n. 39.
[63] [1972] 1 Q.B. 60,63.

Folder
Fr

FRENCH, M.P.
Damages for pre-

Fr
FRENCH, M.P. Damages for pre-contract expenditure

this does not mean that causation is completely excluded, for "the first thing that the plaintiff must show is that the loss which he has sustained was caused by the breach."[64] It is suggested that the American position, which states that pre-contract expenditure is irrecoverable on the ground that the action is based upon the contract and these are not losses sustained as a consequence of the contract, is incorrect. The question is: Is it true to say (as the Americans apparently do) that there is no causal connection between the loss (the wasted expenditure) and either the making of the contract or its breach?

While it may be hard to argue that the expenditure was incurred on the basis of the particular contract between the plaintiff and the defendant, since that contract was not in existence when the expenditure was incurred, it would nevertheless be unreasonable to allow the defendant to escape liability on these grounds. Had the plaintiff never anticipated entering into such a contract the expenditure would not have been incurred, but a contract was anticipated and this provided the basis for the expenditure. On entering the contract with the defendant the expenditure was appropriated to that contract and at that stage no loss had occurred since the expenditure was put to the use for which it was intended. When the

---

64 Anson, <u>The Law of Contract</u> (23rd ed. 1969) 505.

L.C

Folder Fr FRENCH, M.P. Damages for pre-

contract was entered into and the pre-contract expenditure appropriated to that contract there is no reason to draw a distinction between this expenditure and the post-contract expenditure. In both situations the plaintiff has the opportunity to have the value of the expenditure returned to him from the benefits which will accrue from the contract when it is fully performed. If the defendant breaches the contract however this opportunity disappears and the expenditure is rendered useless. It is at this point that the loss arises whether it is post-contract expenditure or pre-contract expenditure, and clearly it is the defendant's breach which has caused the loss.

This was the situation in Anglia T.V. v Reed.[65] By employing certain personnel before the contract with the defendant was entered into the plaintiff took the risk that if no such contract eventuated the loss would fall entirely on his own shoulders. Once the contract with the defendant was entered into however this expenditure was able to be appropriated to that contract by the personnel being deployed in the positions they were hired to fill. At this point of time the expenditure had obviously not been wasted and no loss had been incurred. The situation was in fact substantially the same as if the expenditure had been post-contract. It was the defendant's breach of contract which rendered the expenditure useless and therefore, as Denning M.R. held, there was no reason why

---

[65] Supra, n. 42.

FRENCH, M.P. Damages for pre-contract expenditure

Folder
Fr

FRENCH, M.P.
Damages for pre-

the defendant should escape liability merely because the expenditure in question was incurred before the contract was entered into.

The question of whether pre-contract expenditure could be recovered in an action for breach of contract was raised in two recent unreported cases decided in the New Zealand Supreme Court. In neither case did the court find it necessary to answer the question but there were some interesting observations during the course of the judgments on the causal connection between the loss and the breach.

In Ash v Victor Enterprises Ltd[66] the defendant company, by an oral agreement, employed the plaintiff as a design engineer. The plaintiff left the employer he was working for at the time the agreement was made in order to take up the new position and thereby gave up any rights he had to receive a substantial cash sum on the completion of twenty years service. The plaintiff was dissatisfied with the work given him by the defendant and gave notice to terminate his employment. He then sued the defendant for breach of contract, claiming (amongst other claims which were later abandoned) the cash sum he had forfeited by terminating his previous employment. Relying on the decision in Anglia T.V. v Reed,

---

66 Supreme Court of New Zealand, August 5 1974; (A. 591/70).

Fr FRENCH, M.P. Damages for Pre-contract expenditure

Folder
Fr

FRENCH, M.P.
Damages for pre-

Fr FRENCH, M.P. Damages for pre-contract expenditure

the claim was put on the ground that, by entering into the contract with the defendant, the plaintiff had foregone an opportunity to gain in reliance on that contract and therefore he was entitled to be compensated.

Cooke J. did not consider that the defendant was in breach by not providing the plaintiff with the type of work he had expected under the terms of the oral agreement, since normally the employer is under no obligation to provide work.[67] Cooke J. thought, however, that even if there had been a breach there was still no foundation for the claim. He distinguished the present case from Anglia T.V. v Reed on the ground that "there was in that case nothing equivalent to the election in this case to abandon one contract for another, and because the present is not a case of pre-contract expenditure for the purpose of carrying out a proposed contract."

This conclusion was reached after a consideration of the causal connection between the loss and the breach. Following the approach taken in the Anglia T.V. v Reed case, could it be said, in the present case, that it was the defendant's breach (assuming that a breach had occurred) which caused the loss? There is clearly a distinction between the two cases. In the present case the termination of the former contract was not a necessary

---

[67] Chitty, The Law of Contracts (23rd ed. 1968) 693.

L.C

Folder Fr | FRENCH, M.P. Damages for pre-

part of the performance of the proposed contract as such. Although it was necessary for the plaintiff to terminate one contract before he could enter into the other, this was nevertheless a decision for the plaintiff himself to make. The benefits under the former contract were given up when that contract was terminated and the loss had therefore occurred before the contract with the defendant was entered into. It was the plaintiff's act in deciding to terminate the former contract and to accept a position with the defendant which caused the loss and not the defendant's breach of the later contract. It is therefore suggested that Cooke J. was correct in holding that the rationale used in Anglia T.V. v Reed did not apply in the present case.

The later case of Moola Bar v Brierley-Jones Investments (N.Z.) Ltd[68], although not as significant as Ash v Victor Enterprises Ltd., also raised the issue of pre-contract expenditure. Cooke J. did not find it necessary to consider the "controversial question" because the expenditure claimed by the plaintiff was substantially post-contract. It is relevant however that Denning M.R. is cited as authority for the proposition that the expenditure must be wasted as a result of the breach if it is to be recovered in an action for breach of contract. This arises in the context of the reliance interest but it is still a valid comment with regard to the Anglia T.V. v Reed case.

---

68 Supreme Court of New Zealand, March 18 1975; (A. 18/72).

Fr FRENCH, M.P. Damages for pre-contract expenditure

L.C

Folder Fr FRENCH, M.P. Damages for pre-

Neither of these cases dismissed the possibility that pre-contract expenditure could be recovered in an action for breach of contract. The court in *Ash* v *Victor Enterprises Ltd*, in distinguishing *Anglia T.V.* v *Reed* on the ground that there was no causal connection between the loss and the defendant's breach in this case, not only indicated that it was prepared to consider the issue more fully in the future, but also added support to the argument that the American position is incorrect.

VII CONCLUSION

While it is unfortunate that the court in the cases of *Ash* v *Victor Enterprises Ltd* and *Moola Bar* v *Brierley-Jones Investments (N.Z.) Ltd* did not find it necessary to fully consider the issue of the recovery of pre-contract expenditure, they are an indication that the issue is likely to arise again. If it does there is no valid reason why the recovery of pre-contract expenditure should not be allowed in an action for breach of contract. The American position in denying such recovery is incorrect and, up until recently, the English courts were labouring under the same malady. The *Anglia T.V.* v *Reed* decision was therefore a welcome milestone in stating categorically that pre-contract expenditure could be recovered subject to the principles which pertain to contract damages generally, and in indicating the direction which the law should take in the future.

Fr FRENCH, M.P. Damages for pre-contract expenditure

VICTORIA UNIVERSITY OF WELLINGTON LIBRARY
3 7212 00442807 2

VICTORIA UNIVERSITY OF WELLINGTON
LIBRARY

L
Folder
Fr

FRENCH, M.P.
Damages for pre-
contract expenditure.
333,988

LAW LIBRARY

A fine of 10c per day is
charged on overdue books

LX Fr FRENCH, M.P. Damages for pre-contract expenditure

L
Folder
Fr

FRENCH, M.P.
Damages for pre-
contract expenditure.
333,988

Due 77	Borrower's Name
2/9	[illegible]
2.9	P. [illegible]
11.9	[illegible]
22.9	P. [illegible]
13.10	[illegible]
30-3-81	M. Burrows
[illegible]	I.L. McKay [illegible]
	Swar, Mc[illegible]
5 iii 86	[illegible]

L.C