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Consequential Damages

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Speakers



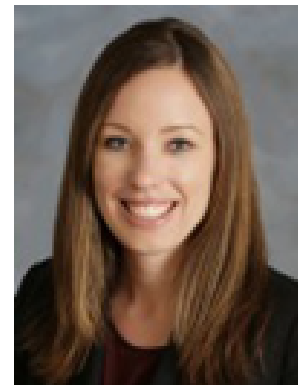
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What Are Consequential Damages (a/k/a Special Damages)?

- Actual damages are either “direct” or “consequential.”
 - Consequential or indirect damages are damages not directly related to the breach of contract but naturally flow from the breach.
 - Would not necessarily be incurred by every injured party experiencing that breach.
- No “bright-line” test for distinguishing consequential from direct damages.

Direct v. Consequential

- **Direct Damages** are damages are those that flow naturally and necessarily from the breach and compensate for loss that is presumed to have been foreseen or contemplated by the parties as a consequence of breach.
 - Based upon what was bargained for in the contract.
 - » unpaid contract amounts
 - » cost to repair defective work
 - » diminution in value
 - *Roanoke Hospital Ass’n v. Doyle & Russell, Inc.*, 215 Va. 796, 801, 214 S.E.2d 155, 160 (Va. 1975).
- **“Special” or “Consequential” damages** are losses to the non-breaching party that “do not flow directly and immediately from the breach, but only from some of the consequences or results of the breach.”
 - must be foreseeable,
 - directly traceable to the wrongful act, and
 - result from the wrongful act.

No Bright – Line Rule

- Consequential Damages are not self-defining.
- Should be defined in the Contract.
 - *Gulf Amer. Indus. v. Airco Indus. Gases*, 573 So.2d 481, 489 (5th Cir. 1990).
 - *Maryott v. First Nat. Bank of Eden*, 624 N.W.2d 96, 103 (S.D. 2001).

Requirements for Recovery of Consequential Damages

- A party seeking consequential damages **must establish** elements that are presumed in the direct damages context.
 - Foreseeability
 - Reasonable certainty
 - Mitigation
- HOWEVER, the degree of proof as to the **amount of damages** is **HIGHER** for consequential damages than for direct damages.
- Consequential damages **must be plead** with greater specificity in most states.

Foreseeability Requirement

- Damages were reasonably foreseeable or within the contemplation of the parties *at the time the parties entered into the contract.*
- Rationale - a party who can reasonably foresee the consequences of a breach of contract can adjust the contract price accordingly to compensate for the risk that is being assumed.
- *Spang Indus.*, 512 F.2d 365, 368 (2d Cir. 1975).
- *Roanoke Hospital*, 214 S.E.2d at 160.

Foreseeability Test

- **Subjective test** - requiring a showing that the particular damages were actually within the contemplation of the contracting parties.
- **Alternative/objective test** - Special damages are recoverable if the special or particular circumstances from which they arise were actually communicated to or known by the breaching party (a subjective test) or were matters of which the breaching party should have been aware at the time of contracting (an objective test).
 - » *Lewis Jorge Const. Mgmt., Inc. v. Pomona Unified School Dist.*, 102 P.3d 257 (Cal. 2004).
 - » *O'Toole v. Northrop Grumman Corp.*, 305 F.3d 1222, 1226 (10th Cir. 2002).
 - » *Berkel & Co. Contractors, Inc. v. Palm & Associates, Inc.*, 814 N.E.2d 649, 658-59 (Ind. Ct. App. 2004).

Burden of Proving Amount of Damages

- Must make a showing sufficient to permit an intelligent and reasonable estimate of the loss.
- Some courts have expressly required the amount of consequential damages to be proven “with reasonable certainty,” while requiring only a “reasonable estimate” of direct damages.
 - » *Compania Embotelladora Del Pacifico, S.A. v. Pepsi Cola Co.*, 650 F.Supp. 2d 314, 322 (S.D.N.Y. 2009).
- Recovery is not be precluded simply because there is some uncertainty as to the precise amount of the damages incurred.

Specific Pleading Requirement

- Federal Rule of Civil Procedure 9(g) and many state rules require parties to specifically plead “special damages.”
- Evidence of special damages is inadmissible if those damages are not specifically pled in the complaint.
- Put in all answers to affirmative defense to knock out a claim for damages.

Duty to Mitigate

- When a contract is breached, the non-breaching party must act reasonably and timely to mitigate its damages.
- Amounts reasonably incurred by a plaintiff to mitigate damages may themselves be recoverable as a form of consequential damages.

Common Construction-related Consequential Damages

- Absent a controlling contract provision, whether these items are recovered is determined through the consequential damages analysis discussed above (i.e., whether the damages were actually contemplated by the parties or otherwise, reasonably foreseeable, and can be proven with reasonable certainty).
 1. Unabsorbed Home Office Overhead
 2. Lost Profits on the Project at Issue (sometimes considered compensable)
 3. Lost Profits on other Projects
 4. Delay
 5. Diminished Bonding Capacity

Common Construction-related Consequential Damages (Con't.)

6. Interest Accrued on Loan While Awaiting Payment
 - » The majority of courts hold that contractors ARE NOT permitted to recover loan-related interest expenditures where these expenses are characterized as consequential damages, as opposed to direct damages.
 - *RAJ Partners, Ltd. v. Darco Const. Corp.*, 217 S.W.3d 638, 649 (Tex. App. 2006).
 - *Cencula v. Keller*, 536 N.E.2d 93 (Ill. App. Ct. 1989).
 - *Dept. of Transp. v. Arapaho Const., Inc.*, 349 S.E.2d 196, 201 (Ga. Ct. App. 1986).
 - *Moore Const. Co. v. Clarksville Dept. of Elec.*, 707 S.W.2d 1, 15 (Tenn. Ct. App. 1986).
7. Additional Fees Paid to Insurers or Sureties

Common Owner/Developer Damages

1. Contractually-Required Variable Expenses
2. Extended Construction Financing Expense
3. Lost Profits
4. Liquidated Damages

Avoiding Consequential Damages By Waiving Them In Advance

- Waiver of Consequential Damages
- Ways Consequential Damage Clause can be invalidated:
 - Bad faith
 - Fraud
- *Long Island Lighting Co. v. Transamerica Delaval, Inc.*, 646 F.Supp. 1442, 1458 (S.D.N.Y.1986) (“A defendant may be estopped from asserting a contractual limitation of consequential damages if the defendant has acted in bad faith.”)
- *Valve Corp. v. Sierra Entertainment Inc.*, 431 F.Supp.2d 1091, 1101 (W.D.Wash.2004) (“A limitation of liability clause may not apply where the party relying on the clause acted in ‘bad faith.’”)
- *Colonial Life Ins. Co. of Amer. v. Elec. Data Sys. Corp.*, 817 F.Supp. 235, 242–43 (D.N.H.1993) (“[A] contractual limitation of liability is not enforceable ... if plaintiff’s claim of fraud, bad faith and/or ‘total and fundamental’ breach is proven at trial.”)

Avoiding Consequential Damages By Waiving Them In Advance

- *City of Dillingham v. CH2M Hill Nw., Inc.*, 873 P.2d 1271, 1275 (Alaska 1994) (“Liability for ‘knowing,’ or ‘bad faith’ breaches can never be limited.”)
- *J.A. Jones Constr. Co. v. City of Dover*, 372 A.2d 540, 545 (Del.Super.Ct.1977) (“Even if a contract purports to give a general exoneration from ‘damages,’ it will not protect a party from a claim involving its own fraud or bad faith.”)
- *Jewish Hosp. of St. Louis v. Boatmen’s Nat’l Bank of Belleville*, 261 Ill.App.3d 750, 199 Ill.Dec. 276, 633 N.E.2d 1267, 1280 (1994) (“Although exculpatory provisions such as this are not given special favor in the law, they are generally held effective except as to reckless or intentional breaches or those committed in bad faith.”)
- *Corinno Civetta Constr. Corp. v. City of New York*, 67 N.Y.2d 297, 502 N.Y.S.2d 681, 493 N.E.2d 905, 910 (1986) (clause limiting liability for delay in construction contract not enforceable if delay caused by bad faith)

Avoiding Consequential Damages By Waiving Them In Advance

- *Psaty & Fuhrman v. Hous. Auth. of City of Providence*, 76 R.I. 87, 68 A.2d 32, 36 (1949) (“If a party to a contract with such a [limitation of damages] clause acts honestly within the fair and legal import of its terms, he cannot be deprived of the benefit thereof unless his conduct indicates bad faith ..., as every contract implies fair dealing between the parties.”)
- *Airfreight Exp. Ltd. v. Evergreen Air Center Inc.*, 215 Ariz. 103 (2007) (As a matter of public policy, a party should not benefit from a bargain it performed in bad faith.)

Delay Damages

- Form of Consequential Damages
- Delay of completion increases both the owner's and the contractor's costs
- Types of delay damages, include:
 - **Compensable delays**: when a party can establish its additional costs attributable to delay such costs are generally deemed recoverable.
 - **Excusable delays**: delays that excuse a contractor's tardiness by allowing for a time extension, but for which the contractor is not entitled additional compensation (i.e. adverse weather condition).
 - **Loss of efficiency/productivity damages**: additional expense in the completion of a work due to a consequence of conditions in the field being different from those the contractor envisioned in accepting the work.

No Damage for Delay Clauses

- Some contracts include a “no damage for delay” clause.
- No damage for delay clauses are generally enforceable.
- Exceptions where the clause is not upheld if the cause of the delay is:
 - The bad faith of the party seeking to enforce the claim;
 - So long in duration that it amounts to abandonment of the contract;
 - Beyond the contemplation of the parties at the time of the contract formation; or
 - The result of active interference of the parties seeking to enforce the clause.
- Example: clause was not enforced due to a finding of abandonment of the contract. *RAI Indus. Fabricators, LLC v. Fed. Ins. Co.*, 2018 U.S. Dist. LEXIS 74612 (N.D. Cal., May 2, 2018)(unpublished) relying on *Opdyke & Butler v. Silver*, 111 Cal.app.2d 912 (1952) and *C. Norman Peterson Co. v. Container Corp. of America*, 172 Cal.App.3d 628 (1985).

Acceleration Costs

- Courts are split as to whether damages for a contractor’s “acceleration” efforts are distinguishable from delay damages allowing for recovery even when there is an enforceable “no damage for delay” clause.
 - *Siefford v. Hous. Auth. of Humboldt*, 223 N.W.2d 816 (Neb. 1974) (disallowing the recovery of acceleration damages under a no-damage-for-delay clause);
 - *Watson Elec. Constr. Co. v. Winston-Salem*, 109 N.C. App. 194 (1993) (allowing the recovery of acceleration damages despite a no-damage-for-delay clause).
- Acceleration damages that do not flow as a consequence of delays may be recoverable.
 - *In United States Indus. v. Blake Constr. Co.*, 217 U.S. App. D.C. 33 (1982), the court recognized the distinction between claims for delay versus disruption and awarded disruption damages to a contractor despite the presence of a no-damage-for-delay clause.

Waiver of Consequential Damages in Project Contracts

- Some contracts include provisions to waive all claims for consequential damages in various sections of project contracts.
- Dispositive Motions can be key effective tools to address key damage issues early in case litigation.
- Contract waiver provisions can be located in different sections so don't be fooled by headings and other damage sections with contract waiver language and always compare with contradicting language and apply key contract language to discern the intent of the parties at the time of contract execution.



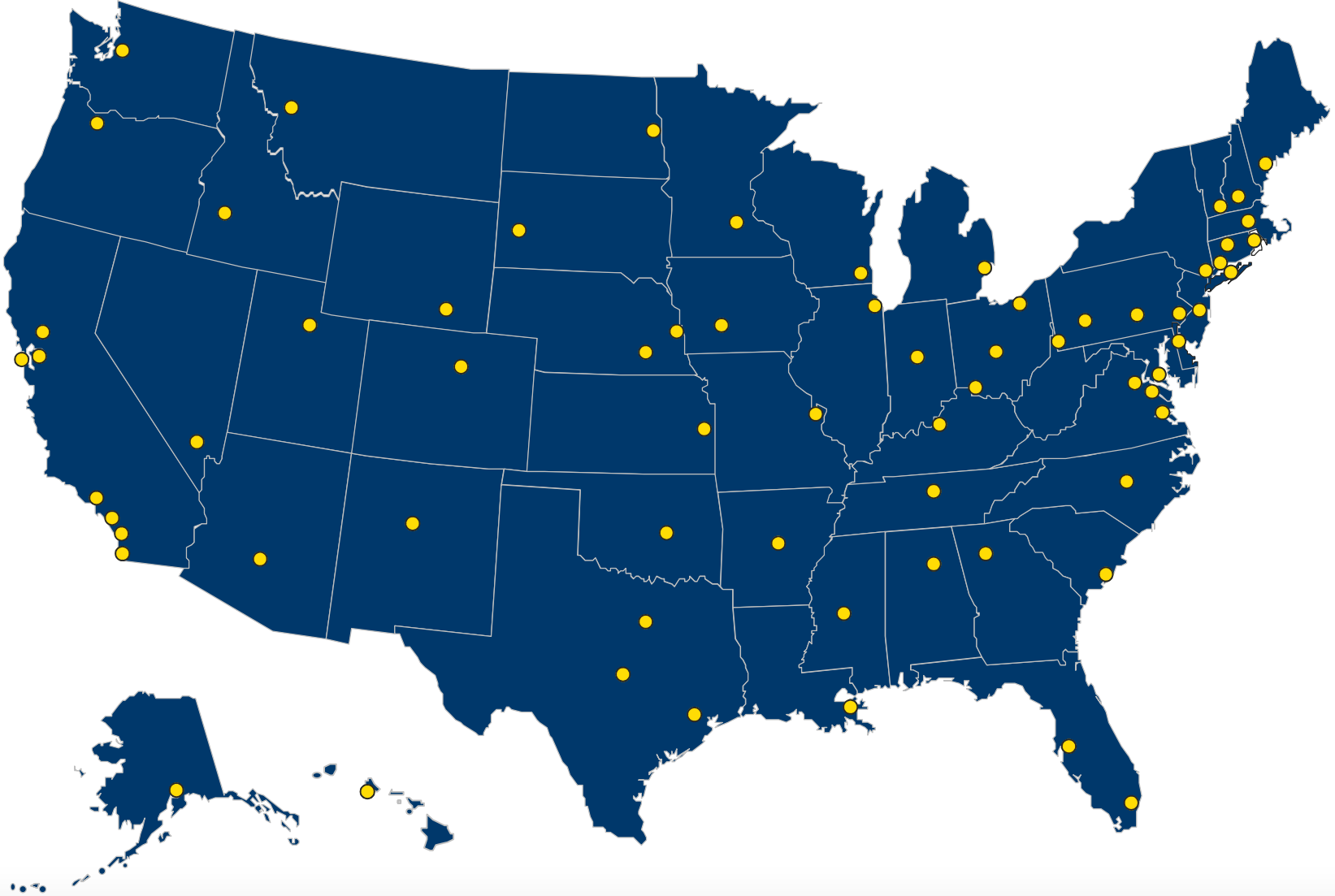
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