

Professional Perspective

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New York Breach of Contract Damages

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Lawyers often put damages analysis in a breach of contract dispute on the back burner because damages are determined at the end of a case. However, an early damages assessment can be crucial to developing a winning strategy. Among other things, expert witnesses are often required to prove or rebut damages; engaging those experts early can help the lawyers develop the key factual evidence.

This article discusses the basic damages recoverable under New York law for breach of contract, and how parties can limit or liquidate those damages by advance agreement.

General Damages

The bedrock principle of contract damages is that “a party injured by a breach is entitled to recover damages that are the natural and probable consequence of the breach.” *APL Co. PTE v. Blue Water Shipping U.S. Inc.*, 592 F.3d 108, 111 (2d Cir. 2010). The two basic categories of damages are general damages and consequential damages. *Schonfeld v. Hilliard*, 218 F.3d 164, 175 (2d Cir. 2000). The winner can also, in rare cases, recover attorneys’ fees and punitive damages. The plaintiff has the burden of proving with a “reasonable degree of certainty” that its damages were caused by the breach. *In re: Residential Capital, LLC*, 533 B.R. 379, 407 (Bankr. S.D.N.Y. 2015).

Benefit of the Bargain and Expectation

General damages compensate a party for the lost benefit of its bargain. The philosophy is that the non-breaching party should be put in the same economic position as if the breaching party had performed. Thus, when a sale of goods contract is breached, the buyer usually recovers the difference between the contract price and the market price for the goods at the time of the breach if the market price was higher. See *Emposimato v. CFC Acquisition Corp.*, 89 A.D.3d 418, 421, (1st Dep’t 2011). If the market price was lower, the buyer has no damages and no claim, because damages are an essential element of the cause of action. *Nielsen Co. (U.S.), LLC v. Success Sys., Inc.*, 112 F. Supp. 3d 83, 97 (S.D.N.Y. 2015).

Recovering damages for breaches of other kinds of contracts can be more complicated. *Latham Land I, LLC v. TGI Friday’s, Inc.* and *Schonfeld v. Hilliard* illustrate the complexity that can arise in proving general damages and the value of creativity in formulating a damages claim. 96 A.D.3d 1327 (3d Dep’t 2012); 218 F.3d 164.

The defendant in *Latham* breached its agreement to construct and operate a TGI Friday’s restaurant on the plaintiff’s land. The contract did not contain a rent acceleration clause and barred consequential damages, but the plaintiff sold the land before the defendant started paying rent. Unable to recover lost rent, the plaintiff claimed the property’s lost market value. An expert testified that there was a market for such properties in the triple-net lease market and that an accepted valuation method existed. The expert calculated what the market value of the property would have been if the defendant had performed. One of the key elements of the expert’s calculation was the expected rent, which plaintiff was precluded from recovering. The trial court held that the claimed damages were barred by the contractual consequential damages waiver. But the Appellate Division reversed, holding that the lost market value constituted general (direct) damages: “the loss asserted here is the very essence of the contract between the parties—i.e., the diminution in value of the actual property defendant promised to improve and lease.” The Appellate Division also held that the plaintiff met its burden of attempting to mitigate its damages by demonstrating it tried and failed to find a new tenant.

Similarly, the Second Circuit in *Schonfeld*, while holding that lost profits were not recoverable, allowed the plaintiff to recover the market value of a license to distribute television despite the fact that expected profits were a key element of the market value. Unlike the court in *Latham*, the Second Circuit categorized the market value damages as consequential, but the contract did not bar consequential damages.

The plaintiffs in *Latham* and *Schonfeld* offered solid evidence of market value, including similar transactions and offers received, thus meeting their burden to show “a stable foundation for a reasonable estimate of the value of the bargain made.” *Ostano Commerzanstalt v. Telewide Sys., Inc.*, 794 F.2d 763, 767 (2d Cir. 1986) (citation and internal quotation marks omitted).

Mitigation

The plaintiff in a breach of contract case must make a reasonable effort to mitigate its damages. See *M. Golodetz Exp. Corp. v. S/S Lake Anja*, [751 F.2d 1103](#), 1112 (2d Cir. 1985). If a plaintiff fails to make a reasonable effort to mitigate, damages will be reduced by the amount that would have resulted from such effort. The mitigation efforts do not, however, need to succeed. Whether the plaintiff's efforts were reasonable depends on the facts.

The Second Circuit has held that the standard for what constitutes a reasonable effort is lower than in other areas of the law. For example, in *APL Co.*, the Second Circuit reversed the District Court's holding that the plaintiff had failed to mitigate, despite the fact the goods involved had spoiled because plaintiff had misunderstood certain regulatory requirements:

[M]issing is an analysis of [plaintiff's] shortcomings against the more forgiving standard accorded a party that has fully performed all of its contract obligations and is thrust into the shoes of the breaching party as it scrambles to mitigate the impact of the breach. The trial court's obligation was to determine whether the mitigation efforts actually chosen in those unaccustomed shoes were reasonable, not whether hindsight suggests that an objectively better choice was available.

[592 F.3d at 112](#).

Reliance and Sunk Cost Damages

A plaintiff can recover reliance damages, or sunk costs, when benefit of the bargain damages cannot be calculated with reasonable certainty. In *re Apollo Air Passenger Computer Reservation Sys. (CRS)*, [720 F. Supp. 1068](#), 1076 (S.D.N.Y. 1989); *In re: Residential Capital, LLC*, [533 B.R. 379](#), 407 (Bankr. S.D.N.Y. 2015). Such damages seek to restore the plaintiff to its pre-contract position. They can include the amounts the plaintiff spent preparing for defendant's performance and debt obligations. *In re: Residential Capital, LLC*, [533 B.R. 379](#), 407 (Bankr. S.D.N.Y. 2015). For example, in *Nature's Plus Nordic A/S v. Natural Organics, Inc.*, [98 F. Supp. 3d 600](#) (E.D.N.Y. 2015), *aff'd*, [646 F. App'x 25](#) (2d Cir. 2016), the court upheld a jury verdict which granted Nature's Plus Nordic an amount it had taken out in loans in reliance on Natural Organics' expected, but failed, performance.

Consequential Damages

Consequential damages differ from general damages because they do not result directly from the breach. *Biotronik A.G. v. Conor Medsystems Ireland, Ltd.*, [22 N.Y.3d 799](#) (2014). While the distinction between general and consequential damages is superficially clear, the "application to specific contracts and controversies can be more elusive." [22 N.Y.3d at 806](#). To classify a particular damages claim, a court looks to "the reasonable contemplation of the parties, the nature, purpose and particular circumstances of the contract known by the parties ... as well as what liability the defendant fairly may be supposed to have assumed consciously, or to have warranted the plaintiff reasonably to suppose that it assumed, when the contract was made." *PNC Bank, Nat. Ass'n v. Wolters Kluwer Fin. Servs., Inc.*, [73 F. Supp. 3d 358](#), 371 (S.D.N.Y. 2014).

Lost profits may be general or consequential damages. In *Biotronik A.G. v. Conor Medsystems Ireland, Ltd.*, a distributor of medical devices sought lost profits from a stent manufacturer for breach of an exclusive distribution agreement. New York's Court of Appeals held the lost profits were general damages. The court said the key question was whether the lost profits "flowed directly from the contract itself or were, instead, the result of a separate agreement with a nonparty." Because the parties' distribution contract "used plaintiff's resale price as a benchmark for the transfer price," the lost profits flowed "directly from the pricing formula" and were direct damages. By contrast, the Southern District of New York held in *Compania Embotelladora Del Pacifico, S.A. v. Pepsi Cola Co.*, [650 F. Supp. 2d 314](#), 322 (S.D.N.Y. 2009) that lost profits for breach of a beverage bottler agreement were consequential damages because they flowed from "collateral business arrangements."

Consequential damages may also include "damages that resulted from the loss of an income-producing asset, the fair market value of which may be based, in whole or in part, on a buyer's projections of what income he could derive from the asset in the future." *Schonfeld*, [218 F.3d 164](#).

Whether a plaintiff should claim lost profits or market value depends on the case. The plaintiff in *Schonfeld* sought both in the alternative. It is sometimes easier to calculate fair market value with reasonable certainty than lost profits. The fair market value under a contract is "the price at which the property would change hands between a willing buyer and a willing seller,

neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.” *Schonfeld*, 218 F.3d at 178. Lost profits “must be capable of measurement based upon known reliable factors without undue speculation.” This is a difficult hurdle, especially when the lost profits are based on projections of future profit.

Punitive Damages

Punitive damages are awarded to punish and deter the defendant. They are not generally recoverable for breach of contract. *Topps Co. v. Cadbury Stani S.A.I.C.*, 380 F. Supp. 2d 250, 261 (S.D.N.Y. 2005). Punitive damages are intended to vindicate public rights. *Rocanova v. Equitable Life Assur. Soc. of U.S.*, 83 N.Y.2d 603, 613 (1994). As such, they are available only “in those limited circumstances where it is necessary to deter defendant and others like it from engaging in conduct that may be characterized as ‘gross’ and ‘morally reprehensible,’ and of ‘such wanton dishonesty as to imply a criminal indifference to civil obligations.’” *New York Univ. v. Cont’l Ins. Co.*, 87 N.Y.2d 308, 315-16 (1995) (quoting *Rocanova*, 83 N.Y.2d at 614). The plaintiff must show the breaching party engaged in conduct that was actionable as an independent tort, of an egregious nature, directed at the plaintiff, and “part of a pattern directed at the public generally.” Tort claims that can qualify include claims that a party fraudulently induced the plaintiff to enter into a contract, or that the party engaged in conduct outside the bounds of the contract designed to defeat it.

In *Rocanova*, the plaintiff sued an insurer for unfair settlement practices in connection with a disability income policy. The plaintiff claimed punitive damages, alleging the insurance company had engaged in a pattern of publicly-directed bad-faith conduct in evading insurance claims. The Court of Appeals rejected the punitive damages claim because the insurance company’s alleged settlement practices did not constitute “a fraud evincing a ‘high degree of moral turpitude’ and demonstrating ‘such wanton dishonesty as to imply a criminal indifference to civil obligations.’” 83 N.Y.2d at 615 (quoting *Walker v. Sheldon*, 10 N.Y.2d 401, 405 (1961)).

A rare breach of contract case in which punitive damages were held available was *Skibinsky v. State Farm Fire & Casualty Co.*, 6 A.D.3d 975 (3d Dep’t 2004). There, the plaintiff alleged the defendant had engaged in a pattern of deceptive conduct by selling lesser policies than those requested by members of the public, while representing the desired coverage had been provided. The Appellate Division held that the widespread nature of the alleged misrepresentations could constitute a fraud on the public that justified punitive damages.

Contractual Limitation of Damages

New York has adopted a freedom of contract approach to clauses that limit parties’ damages: they are generally enforceable, subject to certain limited exceptions. The exceptions include fraud or gross negligence by the party relying on the limitation or the existence of a special relationship between the parties, such as employer and employee. *Colnaghi, U.S.A., Ltd. v. Jewelers Prot. Servs., Ltd.*, 81 N.Y.2d 821, 823 (1993); *Ryan v. IM Kapco, Inc.*, 88 A.D.3d 682, 683 (2d Dep’t 2011); *Johnston v. Fargo*, 184 N.Y. 379 (1906). Moreover, absent language to the contrary, a limitation clause does not apply to misrepresentations made to induce a party to enter the agreement. *Sear-Brown Grp. v. Jay Bldrs, Inc.*, 244 A.D.2d 966, 967 (4th Dep’t 1997). There are also statutory prohibitions on damages limitations for certain types of contracts, such as those involving work done to real property. §§ 5-322.1 et seq., 5-323.

The identity of the parties is important. Courts are more likely to enforce liability limitations agreed upon by sophisticated parties represented by counsel. See *Metro. Life Ins. Co. v. Noble Lowndes Int’l, Inc.*, 84 N.Y.2d 430, 436 (1994). The courts can refuse to enforce a limitation that resulted from unconscionable conduct or a drastic inequality in bargaining power. *In re Lyondell Chem. Co.*, 544 B.R. 75, 85 (Bankr. S.D.N.Y. 2016). But the courts will not void a limitation clause merely because a party has acted in its own economic self-interest. *Morgan Stanley & Co. Inc. v. Peak Ridge Master SPC Ltd.*, 930 F. Supp. 2d 532, 544-45 (S.D.N.Y. 2013).

Consequential Damage Waivers

Courts will generally enforce contract provisions that exclude consequential damages so long as they are not unconscionable. See *MG Hotel, LLC v. Bovis Lend Lease, LMB, Inc.*, 133 A.D.3d 519, 520 (1st Dep’t 2015); U.C.C. § 2-719(3). To demonstrate unconscionability, a party needs to show that the contract was “both procedurally and substantively unconscionable when made”—i.e., that one of the parties lacked a meaningful choice, and the contract terms were unreasonably favorable to the other party. *McNally Wellman Co., a Div. of Boliden Allis v. New York State Elec. & Gas Corp.*, 63 F.3d 1188, 1198 (2d Cir. 1995). Under the New York Uniform Commercial Code, absent unconscionability, clauses that exclude consequential damages will be enforced even if the limited remedy that remains available to the non-breaching

party, such as direct damages, or repair and replacement in a sale of goods contract, fails in its essential purpose. *McNally Wellman Co., a Div. of Boliden Allis v. New York State Elec. & Gas Corp.*, 63 F.3d 1188, 1198 (2d Cir. 1995); N.Y. U.C.C. § 2-719.

Liquidated Damages

Liquidated damages are an agreed fixed payment due for breach. Liquidated damages clauses range from the straightforward per diem amounts often found in construction contracts to the complex economic formulae in swap agreements. Liquidated damages clauses “permit parties to look to the future, anticipate that there may be a breach and make a settlement in advance.” *Jarro Bldg. Indus. Corp. v. Schwartz*, 281 N.Y.S.2d 420, 425 (2d Dep’t 1967). New York enforces liquidated damages clauses so long as the damages are not a “penalty.” *JMD Holding Corp. v. Cong. Fin. Corp.*, 4 N.Y.3d 373, 381 (2005). The reviewing court will consider whether the specified liquidated damages are “at an amount which is reasonable in the 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.” UCC § 2-718(1); see *JMD Holding Corp.*, 4 N.Y.3d 373. It is unwise, therefore, to include any language that suggests that a liquidated damages clause is a penalty.

Courts are more likely to enforce a liquidated damages clause if the contract involves a new business venture or product with little history, such that damages are difficult to ascertain at the time of contracting. New York’s Court of Appeals has noted a growing judicial trend toward enforcement of liquidated damages provisions in contracts between sophisticated parties. *JMD Holding Corp.*, 4 N.Y.3d at 380-81.

An enforceable liquidated damages clause precludes the recovery of any other types of damages, even if such damages are not covered by the liquidated damages clause. *Brecher v. Laikin*, 430 F.Supp. 103, 106 (S.D.N.Y. 1977). Where a contract expressly provides that a party can recover both liquidated and actual damages, the liquidated damages provision is unenforceable. For example, in *U.S. Fidelity and Guaranty Co. v. Braspetro Oil Services Co.*, the Second Circuit voided a liquidated damages provision because the contract also permitted the recovery of actual damages. 369 F.3d 34, 73 (2d Cir. 2004). It explained that “[u]nder no circumstances ... will liquidated damages be allowed where the contractual language and attendant circumstances show that the contract provides for the full recovery of actual damages, because liquidated and actual damages are mutually exclusive remedies under New York law.”

A party that seeks to avoid liquidated damages must prove the existence of one of the limited grounds for denying enforcement. 369 F.3d 34, 73 (2d Cir. 2004). For example, enforcement can be denied if the liquidated damages clause does not provide for the recovery of a sum certain or does not contain a damages formula susceptible to undisputed calculation. In such circumstances, the clause is unenforceable because it fails to achieve the aim of resolving the damages question in advance without significant dispute. See *Chateau D’If Corp. v. City of New York*, 641 N.Y.S.2d 252, 254 (1st Dep’t 1996); *Wells Fargo Bank, N.A. v. LaSalle Bank Nat. Ass’n*, No. CIV-08-1125-C, 2011 BL 218025, at *4 (W.D. Okla. Aug. 23, 2011) (applying New York law). If a liquidated damages clause is voided, the plaintiff can still recover actual damages.

Legal Fees

Legal fees are not normally recoverable unless a contractual clause provides for them. *In re New York Skyline, Inc.*, 471 B.R. 69, 89 (Bankr. S.D.N.Y. 2012). And a court will only award “presumptively reasonable fees.” *LG Capital Funding, LLC v. FLASR, Inc.*, 422 F. Supp. 3d 611, 620 (E.D.N.Y. 2018). Legal fees can also be awarded if the parties agree to arbitration rules that provide for the recovery of legal fees. See, e.g., *Warner Bros. Records v. PPX Enterprises, Inc.*, 7 A.D.3d 330, 330 (1st Dep’t 2004). Many international arbitration rules contain such provisions. See, e.g., *ICC Rules of Arbitration*, Art. 38(1) (2017); *AAA Commercial Arbitration Rules*, R. 48(d)(ii).

Interest

Section 5001 of New York’s Civil Practice Law and Rules provides that a plaintiff can recover 9% pre-judgment interest. N.Y. C.P.L.R. 5001, 5004. Such interest runs from the earliest date of breach and can be substantial in a high-value case. The statutory rate applies unless the parties have agreed to a different prejudgment interest rate in their contract. However, the parties must agree specifically that the agreed rate is for pre-judgment interest. A normal interest provision in a loan agreement does not replace the statutory rate. *Spodek v. Park Prop. Dev. Assocs.*, 96 N.Y.2d 577, 580 (2001).

Indeed, a party that breaches a loan agreement can end up with a judgment that imposes 9% prejudgment interest on both the principal and the unpaid ordinary interest under the loan agreement. New York courts have held that such

recovery does not constitute double-dipping. *HSH Nordbank AG New York Branch v. Swerdlow*, No. 08 CIV. 6131(DLC), [2010 BL 63465](#), at *5 (S.D.N.Y. Mar. 24, 2010), *aff'd sub nom. HSH Nordbank AG New York Branch v. St.*, [421 F. App'x 70](#) (2d Cir. 2011); see also *Spodek v. Park Prop. Dev. Assocs.*, [96 N.Y.2d 577](#), 580, [759 N.E.2d 760](#), 762 (2001).

However, there are questions as to whether the CPLR-mandated interest rates apply in international arbitration in New York, even where New York law governs. See generally N.Y. City Bar Ass'n Int'l Disputes Comm., [Awards of Interest in International Commercial Arbitration: New York Law and Practice](#) (Jun. 21, 2017).

Conclusion

Determining breach of contract damages is rife with uncertainty. Nonetheless, parties and their counsel would be wise to carefully evaluate the available damages—along with limitations—in the early stages of a dispute. This will enable them to avoid surprises and increase the likelihood of a satisfactory result, whether in litigation or negotiated settlement.