Issues coming down the track: Covid-19 and the Assessment of Damages

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Covid 19 and the steps taken by nations across the world to address and arrest its spread has created a new social and economic landscape for large parts of the world. As at the end of April 2020 almost a third of the world is in so called lockdown and large parts of the rest of the world have restrictions in place which in any other time would be perceived as draconian. This new reality is and will continue to impair the performance of some contracts. Force majeure and/or frustration are likely to become familiar (if not over familiar) concepts as parties seek to suggest they should be relieved of contractual obligations (either at all or for a period). But even where liability is established the impact of Covid is likely to be felt when damages are assessed.

That impact might be felt in different ways. A few possibilities are suggested below.

Impact on compensatory principle

When assessing loss for breach of contract the award of damages is designed to put the innocent party in the position as if the contract had been performed (see ***The Golden Victory*** [2007] UKHL 12). This is the so-called compensatory principle. However that decision and ***Bunge v Nidera*** [2015] UKSC 43 make clear that the law should take account of events after the breach that would have reduced the contractual performance and hence the loss. Although this principle will apply most commonly to long term contracts it applies equally to one off contracts as Bunge makes clear.

So if the impact of Covid 19 means that a contract would have been terminated (or discharged by for example force majeure/frustration) after the breach of contract an award of damages must take account of this. Damages should only compensate for the period (if any) whilst contractual performance would have been provided.

The compensatory principle may not only take account of such contingencies. In ***Flame SA v Glorywealth*** [2013] 2 Lloyd's rep. 653 it was said that a claimant seeking damages for the anticipatory repudiation of a long term contract had to prove on the balance of probabilities that they would have been able to perform when the time came for performance by them. If Covid 19 prevents the claimant from being able to perform it may prevent or limit the damages awarded. It seems likely this decision is limited to cases of anticipatory breach (see the recent Court of Appeal decision in ***Classic Maritime v Limbungan Makmur SDN*** [2020] 1 Lloyd's Rep. 178). That decision may cast doubt on Flame SA altogether; it seems the current events will give rise to ample opportunity to test the true scope of the principle.

Is Covid 19 related loss recoverable?

Damages are usually limited to those types of loss which arise naturally, according to the usual course of things, from the breach or those which may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it (see ***Hadley v Baxendale*** (1854) 9 Ex. 341).Thus damages do not usually extend to types of loss resulting from improbable results of the breach, even if such losses were foreseeable in the most general sense. Such losses are too remote too be recoverable. It may even be required that the contract breaker can be said to have assumed responsibility for the particular loss which had occurred (see ***Transfield Shipping Inc v Mercator Shipping Inc, The Achilleas*** [2009] 1 A.C. 61).

The only exception is where special information is conveyed to the contract breaker at the time of concluding the contract and even then the liability is limited to the losses which would ordinarily flow under the special circumstances which were communicated. However so long as the type is of loss of a kind which is recoverable it is irrelevant that the extent or scale of the loss itself is unusual (see ***Parsons v Uttley Ingham*** [1978] QB 791).

So, if the impact of Covid 19 means that the losses sustained by a party are much greater than losses than would ordinarily arise, are such losses recoverable? For example where Covid 19 restrictions have meant that certain good and services which have not been supplied are much more expensive or impossible to replace can losses be assessed by reference to the now much increased cost of sourcing a replacement? Where a replacement goods or services are unavailable can the knock on/consequential losses be claimed where the absence of the market is a function of the Covid restrictions? Are

such losses of a type ordinarily arising from the usual course of things and/or of a type within the contemplation of both parties as the probable result of the breach ?

Each dispute will turn on its own facts. However it should be noted that typically losses arising out of market movements are recoverable even if the scale of the loss is unusual (although the minority judgment of Lord Rodgers in the Achilleas (above) suggests limits to this proposition). So insofar as the pandemic and its consequences have caused collapses or spikes in markets these facts alone are unlikely to make an award of damages based on unusual market conditions as too remote.

Mitigation/benefits

Damages are assessed as if the claimant acted reasonably so as to minimise the loss caused by a breach of contract, even if in fact it did not act reasonably. Moreover where the claimant does take steps to mitigate the loss to him consequent upon the defendant's wrong and these steps are successful, the benefit accruing from the claimant's action is to be brought into account when assessing loss. This is so even if the steps taken exceeded what might be reasonably expected/required (see ***British Westinghouse Electric Co Ltd v Underground Electric Railways Co of London Ltd*** [1912] AC 673). However this final statement needs some qualification in the light of the decision of the Supreme Court in ***Fulton Shipping v Globalia*** [2017] 1 WLR 2581 which requires that acts only qualify as mitigation so as to be taken into account if they are both factually and legally caused by the breach.

The concept of reasonableness in this context does not impose a heavy burden. Parties are not expected to take speculative risks or to act in a way which might be contrary to the general business interests. In uncertain economic times it seems unlikely that parties will be treated as having acted unreasonably lightly. For many commercial parties their options will be limited.

More potential difficulties arise where parties have taken active steps, apparently to replace lost transactions, where those steps are different to the lost transaction. For example where the breach by a counter party frees up capacity so as to allow the innocent party to fulfil one off contracts for governments/states/regions are these to be regarded as acts of mitigation? Are the requirements of legal and factual causation set in ***Fulton*** met?

Similarly where the claimant receives a subsequent benefit which was caused by the breach that benefit it is to be taken into account. The changes caused to the economic landscape caused by the impact of Covid 19 are such that it is possible to envisage that some transactions, if they had been performed, would have given rise to considerable losses. This might be because the value of the asset has fallen (due to a collapse in demand caused by the global restrictions) or because the lost transaction would have been loss making. In such cases the breach/non performance might be said to have conferred a benefit. However in most cases it will be hard for the contract breaker to establish that the benefit was both legally and factually caused by the breach. The collapse in the market was not caused by the breach and so ordinarily loss should be assessed using traditional measures without reference to any change in the value of the goods/services to be provided. As always, much will depend on the facts of each case.

Other damages issues (aside from those discussed above) are likely to rear their head in the disputes which will inevitably follow such a profound economic shock to the system.

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"Really attuned to the client, very clear in his thinking and very sympathetic to the client's case. He brings clarity and a sense of humour, which makes him delightful to work with." (Chambers & Partners UK, 2020)

Simon Croall QC is Head of Quadrant Chambers. He is an established commercial silk who has appeared in every court (including recent appearances in the Supreme Court). He is a sought after trial advocate as well as being respected in the appellate courts. In recent years much of his work has been in the context of International Arbitrations.

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