It makes sense to be aware of what is potentially recoverable before incurring the significant costs of pursuing a claim.

Here, we cover the basics you need to know on contractual damages including the basis of the calculation, mitigation, interest and practical steps to protect your position.

**Overview**

- What is meant by damages?
- How much can I recover?
- What is expectation loss? What is reliance loss?
- What is the difference between direct loss and indirect loss and why is this relevant?
- What are negotiating (Wrotham Park) damages?
- What is mitigation?
- Am I entitled to interest on the damages?
- Can I recover wasted internal management costs?
- Practical points

**Overview**

In this article, we focus on contractual damages.

It may be that there is a choice to claim damages on a different basis - in tort, as an alternative to, or in addition to contractual damages. Remember that the measure of damages in tort is different to the measure that applies for contractual damages - the tortious measure is not covered in this article.
Where liability is proven in contract and, and the breach of contract also amounts to a tort, the contractual measure of damages will apply.

**What is meant by damages?**

Damages are what you will be entitled to recover in principle if you can prove your claim, unless you have agreed an applicable exclusion or limitation of liability in the contract.

Exclusion clauses can be agreed by the parties to a contract in order to limit or exclude contractual liability that would otherwise arise. We cover this in more detail in our article *The Basics: Limiting and excluding liability for breach of contract.*

**How much can I recover?**

Contractual damages are intended to compensate for the loss suffered i.e. generally, to put you in the position you would have been in, if there had been no breach of contract and the contract performed.

**What is expectation loss? What is reliance loss?**

- **Expectation losses** or damages provide compensation to put the "innocent" party in the position they could have expected to be in, if the contract had been properly performed.

  As an example, this could be the cost of any remedial works, or any difference in cost when paying for the services that should have been provided.

- Sometimes, (less commonly) **reliance losses** or damages can be claimed e.g. when it is impossible to predict with any certainty the profit that would have been made if there had been no breach of contract. In that case, a claimant may be able to recover wasted expenditure incurred in reliance on performance of the contract.

  An example from a well-known case arose when an actor was double-booked, resulting in commitments in both the UK and USA at the same time. He pulled out of the UK show (a play that was to be filmed) which then had to be abandoned - the television company was able to recover the money it had spent (and therefore wasted) in preparation for recording the show including the fees of the director, the designer and the stage
It is not possible to recover both expectation and reliance losses - this is to avoid double recovery.

**What is the difference between direct loss and indirect loss and why is this relevant?**

In order to be recoverable, the loss must be foreseeable at the date the contract was entered into (not the date of breach). Understanding the difference between direct and indirect losses will help you in negotiations, and also to assess potential exposures if a breach of contract occurs.

- **Direct loss** means loss flowing naturally from the breach.
- **Indirect loss** (also known as consequential loss) means losses that:
  - do not flow naturally from the breach; and
  - arise from particular (unusual) circumstances that the parties knew or should have known about at the time the contract was entered into.

If they are foreseeable, both direct and indirect losses are recoverable in principle, but many contracts will seek to exclude liability for indirect or consequential losses, as referenced in our article on excluding liability.

**What are negotiating (Wrotham Park) damages?**

In certain cases, negotiating damages (previously known as Wrotham Park damages) may be recoverable, being the amount the defendant would have paid (hypothetically) if, before any breach by the defendant, there had been a negotiation resulting in a payment to the claimant by the defendant in return for the release of the relevant obligations.

When negotiating damages will be recoverable is not entirely clear from the case law, but the Supreme Court has recently held that this approach will not usually be appropriate for breach of contract claims, where damages are usually based on actual loss. However, in principle, negotiating damages can be awarded for breach of contract "where the loss suffered by the claimant is appropriately measured by reference to the economic value of the right which has been breached, considered as an asset".

Practically, this measure of damages will rarely apply.
**What is mitigation?**

A claimant or potential claimant should take reasonable steps to reduce any losses; in other words, to **mitigate** the loss.

As an example, if an employee is dismissed and starts a claim for unfair dismissal, he or she must take reasonable steps to find a new job as soon as possible, in order to reduce the loss potentially recoverable from the previous employer.

If a claimant fails to act reasonably in terms of mitigation, any damages award may be reduced to reflect the reduction of the loss that would have resulted if the claimant had taken reasonable steps to mitigate.

Continuing the example above, if the ex-employee has a suitable job offer but then delays the start date for two months in order to travel, (in the absence of exceptional circumstances) he/she will not be able to recover loss of income for those two months.

**Am I entitled to interest on the damages?**

In most cases, yes but not automatically.

In many cases, if a contract does not provide a substantial remedy for late payment, then a statutory rate of interest will apply - where the Late Payment of Commercial Debts (Interest) Act 1998 applies, this is currently 8% over base rate.

**Can I recover wasted internal management costs?**

In terms of recoverability, internal costs following a breach of contract generally fall into two separate categories.

- staffing costs for those who cannot do their normal job as they are spending time dealing directly with the consequences of the breach:
  - **For example:** when providing services to A, B cracks A's water pipe causing a major leak. Various employees of A have to spend time dealing with the leak and organising/carrying out repair works.
  - Such costs are in principle recoverable as damages.
- Staffing costs for people involved in preparing and pursuing a claim for breach of
contract:
  - **For example**: once the repair work to the pipe is completed, some employees of A spend time working on the preparation of a claim against B to recover losses caused by the damage to the water pipe.
  - These costs are not recoverable as damages (and are unlikely to be otherwise recoverable).

**Practical points**

1. When negotiating contract terms, consider the extent to which you would like to limit liability (if at all).
2. Keep organised clear records of costs/expenses incurred, ensuring adequate itemisation and detail - dates and receipts are important if you need to prove a claim.
3. Where internal time is spent in relation to any aspect of the dispute, keep comprehensive records to include dates, times, personnel involved and the work that was being carried out.

These are good working practices from any perspective and they will certainly save you time and costs at a later stage if a claim arises.

If you have any queries on this or related topics, please contact Ashley Pigott or Catherine Naylor.

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