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UK: "Negotiating damages" and *Wrotham Park* before the Supreme Court.

Morris-Garner v One Step Ltd [2018] UKSC 20 is a landmark UK Supreme Court decision concerning English law on damages for breach of contract. It deals with when a party can obtain a sum equivalent to that which would have been paid by the party in breach to release itself from the relevant obligation. It has particular consequences for breach of certain types of obligation;specifically those relating to control of assets, or other property (such as land, IP or confidential information).

Background – what are "negotiating damages"?

Under English law the traditional measurement of damages for breach of contract is that which would put the claimant in the same position as it would have been in had the contract been performed. As part of this it is necessary to identify the economic loss suffered by a claimant to be compensated. Generally speaking, it also, therefore, follows that where no such loss can be established, any award of damages will be nominal.

However, in recent years, a line of cases have appeared to indicate that, in certain circumstances, a claimant may be entitled to a payment of damages which, rather than being referable to the claimant's loss in the conventional manner described above, is to be measured by reference to a (hypothetically) negotiated sum which would have been paid by the defendant to secure a release of the obligation in question.

Similar awards have long been available under English law for tortious violations of *property* rights (such as trespass to land, or patent infringements), and, as shown by the case of *Wrotham Park v Parkside Homes Limited,*[1] in lieu of an injunction in cases involving the breach of a negative covenant over land. In *A-G v Blake*,[2] however, the House of Lords indicated that what had since commonly been referred to as *Wrotham Park* damages[3] may be available in cases of breach of contractual rights more generally.[4] And, subsequently, for example, there have been cases in which damages have been awarded on the basis of a hypothetical release fee for breach of a confidentiality agreement,[5] or where a defendant breached an agreement not to use its copyright in a certain way.[6]

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[1] [1974] 1 WLR 796. The pronunciation of "Wrotham" is "Rootam".
[2] [2001] 1 AC 268.
[3] The term "negotiating" damages is used here for consistency with the Supreme Court's terminology. As will become clear from what follows, and paragraph 3 of the Supreme Court's judgment, it sees the use of "Wrotham Park damages" as potentially confusing in light of the correct treatment of the authorities.
[4] *Blake* was not, however, a case which was directly concerned with negotiating damages; instead it is direct authority for the proposition that in exceptional circumstances an account of profits can be ordered as a remedy for breach of contract. That, different, point was not one which was under consideration in *One Step*.
[5] *Vercoe v Rutland Fund Management* [2010] EWHC 424 (Ch).
[6] *Experience Hendrix LLC* [2003] EWCA Civ 323.

But the question those cases have given rise to is what the precise circumstances are which justify such a remedy in relation to a breach of contract, and whether it is even possible to reconcile such an approach with more conventional assessments of damages and loss as discussed above.

The facts and issues in *One Step*

These were the precise matters which arose in *One Step*. The case, in short, involved the sale, by the first defendant, of her share in the claimant company (One Step); which was the vehicle for running a business providing support for young people leaving care. In connection with that disposal, the first defendant entered into a (valid) contract containing non-compete, non-solicitation and confidentiality covenants with the claimant (the second defendant, who had been employed by the claimant but left upon the disposal, did likewise). The defendants had, however, set up their own company which they then used to compete (successfully) with the claimant.

The claimant commenced proceedings alleging, amongst other things, breach of those covenants. At first instance[7] the judge found that there had been various breaches. Moreover, he was prepared to make an order that the claimant was entitled to damages for such amount as would notionally have been agreed by the parties, acting reasonably, as the price for releasing the defendants from their covenants. He saw this as being justified principally on the basis that the claimant would have difficulty in identifying the financial loss suffered as a result of the defendants' wrongful competition (although the claimant had attempted to do so as part of its claim).

Before the Court of Appeal, the defendants argued that such an award should only be made where the claimant is unable to demonstrate identifiable financial loss and where it is necessary to avoid any manifest injustice. The Court of Appeal[8] declined to accept such restrictions. It decided, instead, that the test was simply whether such an award was the just response to any particular case; with the difficulty of showing loss in the ordinary sense being something which could be taken into account in that assessment by the trial judge. The Court of Appeal also regarded other factual features of the case, such as the deliberate nature of the breaches, as being relevant to this assessment, and as further justifying the award. It refused to interfere with the judge's order and dismissed the defendants' appeal.

The Supreme Court's decision

On 18 April 2018, the Supreme Court held that the approach of the lower courts was erroneous and, instead, set out a new, authoritative, statement of the circumstances in which negotiating damages may be awarded for a breach of contract. Its decision is contained in a judgment by Lord Reed with which three of the other Supreme Court Justices agreed.[9] Numbers in square brackets which follow are references to paragraphs in Lord Reed's judgment.

Lord Reed's approach was to build up, from first principles and a survey of the cases in which similar awards have been made, the appropriate boundaries of such a remedy. He started by referring to the authorities which establish that, in English law, tortious damages amounting to a reasonable sum for wrongful use of property can be awarded

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7 [2014] EWHC 2213.
8 [2016] EWCA Civ 180.
9 Lord Sumption gave a separate judgment, in which he offered his own reclassification of the preceding authorities. His approach was not, however, followed by the majority. For brevity, and because Lord Reed's judgment represents the authoritative statement of the law, no more is said here in relation to that opinion. For those interested in a potted summary of Lord Reed's judgment, a useful summary of his main conclusions can be found at paragraph [95] of his judgment.

where such interference with property has occurred, and irrespective of any diminution of the value of that property (sometimes known as “user damages”) [25-30]. Next (after a short survey of the basic principles governing damages awards in breach of contract cases generally [31-40]) Lord Reed then examined a number of cases, involving tortious interference with property rights or breach of restrictive covenants over land, of which *Wrotham Park* itself was one. Lord Reed identified that in those circumstances, when exercising its specific *statutory* powers to grant damages in lieu of an injunction (as distinct from a common law claim for breach of damages), the court has also been prepared to grant a sum for an amount which might fairly have charged for the voluntary relinquishment of the right in issue [41-63].

He then turned to *Blake* and the cases which had followed it, which had appeared to open up the possibility of the award of such damages for breaches of contract more generally. Lord Reed subjected these cases to critical analysis [64-90]. In short, he was not prepared to categorise them as a significant extension to what had gone before or as authority for opening up an award of negotiating damages on the basis of wider factors such as whether it was difficult to prove conventional loss, or the degree to which the breach was deliberate [90].

Instead, in respect of a common law claim for breach of damages, Lord Reed identified the real question as simply being the need to identify the circumstances in which negotiating damages can correctly be said to be a measure of loss suffered by the claimant. [91]. With that in mind he said that what his preceding discussion *did* illustrate was that circumstances can exist where a breach of contract results in the loss of a valuable asset created or protected by the right which was infringed, as for example in cases concerned with the breach of restrictive covenants over land, an IP agreement, or a confidentiality agreement. These cases he saw as closely analogous to “user damages” cases in which the defendant has taken something for nothing, for which the claimant is entitled to require payment [91-92]. Lord Reed then went on to emphasise that what was important in this context was that the contractual right needs to be of such a kind that breach can result in an identifiable loss equivalent to the economic value of the right considered as an asset. Whilst that is something true of some contractual rights, such as those to control the use of land, IP or confidential information, it would not be true of all [93].

Applying the above to the circumstances of the case before it, the result was that the Supreme Court overturned the lower courts’ decisions. The claimant’s interest in the defendants’ performance of the relevant covenants was solely commercial and not one where the breach had resulted in the loss of a valuable asset created or protected by the right which was infringed [96-99]. In this regard although the case did involve the breach by the first defendant of a confidentiality covenant (which might have been considered to be of the requisite character), Lord Reed observed that in reality the claimant’s loss was the cumulative result of breaches of a number of obligations of which the non-compete and non-solicitation were the most significant [99] (those not being of the requisite character). The end result was, therefore, that the case was returned to the trial judge to assess damages on the basis of the financial loss actually sustained by the claimants.

Conclusions

The Supreme Court's decision is of great significance in its treatment of the availability of negotiating damages for breach of contract. It clears away the ambiguity, and analysis, of previous case law in favour of a new, rationalised test which focuses on the need to identify a contractual obligation which has created, or protects, an asset equivalent to a property right. By contrast, in the more "usual" case a contractual obligation will create a "commercial" interest, damages for breach of which is to be measured in the usual way. In this way, the Supreme Court's approach is more focused, principled and restrictive than the opaque authorities following *Blake*; of which the Court of Appeal's approach was, arguably, a prime example. It is now clear that this is a remedy applicable in certain circumstances only.[10]

There may, of course, be scope for future argument over whether an obligation falls within the scope of the Supreme Court's test but the judgment does provide some useful indications. Non-compete, and non-solicitation, covenants of the type in issue were regarded as "commercial" interests and so are not of the requisite character for an award of such damages. Contractual rights such as those to control the use of land, IP or confidential information *do*, however, appear to be of the requisite character. The upshot is that, in relation to breaches of contractual rights which are capable of meeting the test laid down by the Supreme Court, *One Step* is likely to become a key case relied upon by claimants in future. That is because the judgment is authoritative *confirmation* that such an award is available in such situations. Further, whilst, in such cases, there is nothing precluding a claimant from also seeking an additional (conventional) award of damages for any actual loss suffered, what makes *One Step* doubly useful for a claimant (where *One Step* applies) is that an award of negotiating damages can be sought even if that (conventional) award would otherwise be unavailable by reason of there having been no actual loss on the claimant's part.

Click here for a copy of the Supreme Court's judgment.

[10] In relation to any concerns that a more restrictive approach may prejudice claimants in cases where negotiating damages are not available and where there are otherwise difficulties in proving precise measurement of loss, Lord Reed appeared to have amelioration of such difficulties in mind when making comments regarding the degree to which the law accommodates imprecision in the same: see [37-39].

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