

THE GLOBAL DAMAGES
REVIEW

Editor
Errol Soriano

THE LAWREVIEWS

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REVIEW

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PREFACE

Rules set boundaries on what is permissible damages evidence. For example, most jurisdictions have established value definitions (fair market value, fair value, etc.) that apply in certain circumstances. Some of these rules have been codified as regulations; others have evolved from a long line of court decisions.

The judiciary monitors and refines the boundaries for evidence on damages, and it is incumbent on litigators to keep abreast of these developments and to continually assess the possible ramifications for their cases.

In this, the inaugural edition of *The Global Damages Review*, we survey the codified rules and common law principles underpinning the presentation of damages evidence. We also summarise recent common law decisions that provide new or improved guidance on these frameworks.

This first edition summarises principles governing the quantification of expert financial evidence in select common law jurisdictions, including the United States, the United Kingdom, Canada and Australia, and highlights important precedents from recent case law in each of the jurisdictions.

The intention is that this inaugural edition will provide the reader with foundational information highlighting the issues that arise with this type of evidence, and each jurisdiction's approach to managing these issues.

Subsequent editions of *The Global Damages Review* will build on the foundation set in this first edition, by delving deeper into concepts underpinning damages quantification, and by providing summaries of important common law decisions handed down during the year.

Please feel free to contact me with any comments or suggestions.

Errol Soriano

Duff & Phelps

Toronto

November 2018

Part I

GENERAL PAPERS

GLOBAL PRINCIPLES OF COMPENSATORY DAMAGES

*Gary J Mennitt, May K Chiang and Selby P Brown*¹

I GENERAL PRINCIPLES

Whether in civil law or common law jurisdictions, the general principle underlying compensatory damages is largely the same: such damages are awarded to put the innocent party in the position it would have been in had the harm not occurred. *Black's Law Dictionary*, a frequently cited legal dictionary in the United States, defines compensatory damages as '[d]amages sufficient in amount to indemnify the injured person for the loss suffered'.² This general principle finds a variety of applications across jurisdictions, factual applications and areas of law.

This chapter will provide some general background on compensatory damages around the world. While not meant to be an exhaustive survey, we endeavour to provide the reader with a basic understanding of the contexts in which compensatory damages are awarded, and how an injured party proves entitlement to the damage amount. Subsequent chapters of this volume will provide more detailed information concerning damage awards in various jurisdictions.

II RESTORING THE INJURED PARTY TO PRE-INJURY STATUS

i Breach of contract

Where a breach of contract is at issue, compensatory damages are designed to place the injured party in the position it would have enjoyed if the contract had not been breached. Such damages are often referred to as 'expectation' or 'benefit of the bargain' damages. In most jurisdictions, this means that the injured party may recover for direct losses owing to the breach of the contract. In a commercial contract setting, lost profits may also be recoverable as compensatory damages, but proving lost profits with the requisite degree of certainty can be difficult and jurisdictions differ with respect to the likelihood of an award of lost profits.

In Australia, a common law jurisdiction, commentators have carefully noted that 'the same situation' does not necessarily mean 'as good a financial position'.³ A monetary substitute

1 Gary J Mennitt is a partner, and May K Chiang and Selby P Brown are associates at Dechert LLP.

2 *Black's Law Dictionary* (10th ed. 2014).

3 Nick Christopoulos, Jack Fan, 'When Can Rectification Costs Be Recovered as Damages for Breach of Contract – The Australian High Court Clarifies', 4 *Const. L. Int'l* 33, 33 (2009).

for performance, then, may not be as lucrative as actual performance of the contract, given that the breach may have caused the injured party's assets to lose their own value, and the fact that the injured party has a duty to mitigate damages.⁴

In Brazil, a civil law jurisdiction, compensatory damages for breach of contract account for both actual loss and future lost profits.⁵ In Russia, another civil law jurisdiction, direct losses and lost profits are recoverable, but lost profits have been particularly difficult to prove.⁶ Furthermore, Russian courts are empowered to reduce the scope of damages if the injured party increased the amount of damages or failed to take reasonable measures to reduce it.⁷

In the United Kingdom, compensatory damages for a breach of contract take the form of 'expectation damages': the injured party is awarded the net loss, which is calculated by quantifying the harms caused by the breach, and then deducting any benefits resulting from the breach.⁸ Such losses can include costs incurred from the breach and the profits that the claimant would have earned but for the breach.⁹ Where it is impractical to prove lost profits, the injured party is entitled to the rebuttable presumption that the venture would have broken even.¹⁰

Though Spain is a civil law country, it recently adopted the common law approach to compensatory damages. Therefore, following a breach of contract, the claimant may recover the costs or expenses it incurred as a result of the breach, and may also be awarded lost profits.¹¹

In Singapore, courts look first to see whether the contract contains a provision for liquidated damages, which fixes the sum of money payable to the non-defaulting party in the event of a breach.¹² If the contract does not have a liquidated damages clause, then the court may award 'unliquidated damages', which essentially function as compensatory damages – they put the party in the position it would have been if the contract had been performed fully.¹³

4 Pauline Ridge, 'The Assessment of Contractual Damages – Ruxley Electronics in Australia', 17 RLR 132 (2009); Brendan Sweeney, 'The Role of Damages in Regulating Horizontal Price-Fixing: Comparing the Situation in the United States, Europe and Australia', 30 *Melb. U. L. Rev.* 837, 874 (2006).

5 Leonardo Canabrava, Lucas Spadano, Ana Paula Lages, Luiza Tângari, Bernardo Santos, Bruno Augustin, Thiago Costa Neto and Fernanda Andrade, 'Contracts, negotiation and enforcement in Brazil: overview', *Practical Law Country Q&A* (1 August 2018).

6 Ian Ivory and Anton Rogoza, 'Damages for breach of contract: a Russian and English law comparison', *Practical Law UK* (19 January 2011).

7 Clare Connellan, Elizabeth Oger-Gross and Angélica André, 'Compensatory Damages Principles in Civil- and Common-Law Jurisdictions – Requirements, Underlying Principles and Limits', *Global Arbitration Review, Guide to Damages in International Arbitration* (2nd edition) (citing Russian Federation Civil Code, Article 404).

8 Adam Kramer, 'Damages for Breach of Contract: An Overview', 1, *Practical Law UK* (2018).

9 *id.*

10 *id.* at 3.

11 Antonio Sánchez Cerbán, 'Contracts, Negotiation, and Enforcement in Spain: Overview', *Practical Law Country Q&A* (1 September 2018).

12 Ramesh Selvaraj and Sean Tseng, 'Contracts, Negotiation, and Enforcement in Singapore: Overview', *Practical Law Country Q&A* (1 August 2018).

13 *id.*

ii Tort and personal injury

Similarly, in the personal injury context, compensatory damages seek to restore the injured party to his or her pre-injury condition. While many countries follow this general principle,¹⁴ jurisdictions differ in the types of losses they consider when awarding compensatory damages for tort. Canada and the United Kingdom provide instructive examples.

To restore a plaintiff to his or her pre-accident condition in Canada, courts look at both non-pecuniary losses such as pain and suffering, as well as the plaintiff's pre-accident financial condition.¹⁵ Courts consider both the past financial loss and the prospective financial loss.¹⁶ If a future loss may result owing to the defendant's wrongful conduct, courts will consider this future contingent loss against the probability of its occurrence; it may be added to the total compensatory damages award on a *pro rata* basis.¹⁷

In the United Kingdom, the injured party is entitled to be returned to the position that it would have been in had the tort not been committed.¹⁸ If the claimant receives benefits under an insurance policy, those benefits are irrelevant to the damage award.¹⁹ Compensable losses may be monetary or non-monetary.²⁰ Courts in the United Kingdom recognise a wide variety of monetary losses: injured parties have recovered for the reasonable cost of repair to damaged goods, loss of anticipated profits, and wasted staff time for having to respond to a significant disruption in business owing to the injury.²¹

III PROVING ENTITLEMENT TO COMPENSATORY DAMAGES

To receive an award of compensatory damages, the injured party must show that the injury in question actually caused the damages sought. The seemingly universal prerequisite of causation requires a direct link between the defendant's conduct and the plaintiff's injury. In some cases, the injured party will be required to rebut the wrongdoer's claim that the injury was caused by a different force. It is also a common concept that an injured party's attempts to obtain damages may be thwarted, at least in part, where the injured party did not take reasonable steps to ensure the damages were not greater than necessary. The concepts of causation and mitigation are discussed further below.

i Causation

Under Russian contract law, 'the non-breaching party must prove the fact and amount of losses and that the losses were caused solely by the breach of the contract', which is difficult to prove. If the damages were caused partly by the breach of contract and partly by something

14 See, e.g., Brendan Sweeney, 'The Role of Damages in Regulating Horizontal Price-Fixing: Comparing the Situation in the United States, Europe and Australia', 30 *Melb. U. L. Rev.* 837, 873-74 (2006); *In re Methyl Tertiary Butyl Ether (MTBE) Products Liability Litigation*, 643 F. Supp. 2d 446, 455 (S.D.N.Y. 2009).

15 D. Bruce Garrow, Do-Ellen S. Hansen, Meredith L. Parkes, 'Damages for Personal Injury or Wrongful Death in Canada', 69 *J. Air L. & Com.* 233, 235 (2004).

16 *id.*

17 Paul Dufays, 'Introducing Provision Damages for Personal Injuries in Canada', 6 *Dalhousie J. Legal Stud.* 1, 2 (1997).

18 Practical Law Dispute Resolution, 'Damages in tort: an overview', 1 (2018).

19 *id.* at 2.

20 *id.* at 1.

21 *id.* at 2, 5.

else, courts will reduce the damages that the breaching party must pay. ‘If the party fails to prove the exact amount of losses, but proves the fact that the losses were incurred, the court must reasonably define the amount of losses by itself.’²²

The Brazilian Civil Code generally requires a causal link between the act or omission attributed to the party in default and the consequence suffered by the innocent party.²³

Law in the United States similarly generally requires a claimant to establish that the compensatory damages sought were suffered as a consequence of the claimed violation of tort law or a contract.²⁴ American courts typically require a plaintiff to establish that the damages were proximately caused by the defendant’s conduct. In other words, while the damages must not have happened but for the defendants’ bad conduct, they cannot be so remote that they cannot be directly traced to the wrongful conduct, and they must not be the result of other intervening causes.²⁵ On the other hand, there may be multiple proximate or ‘but-for’ causes of an injury, and the law of apportioning damages and seeking contribution or indemnity from others jointly or partially liable is generally a matter of state law.²⁶ This is so in both contract and tort law.²⁷

English and Canadian law share substantial overlaps regarding causation. Canadian personal injury law requires the injured party to show both legal and factual causation. Legal causation requires proof that the ‘type or class of injury [was] a foreseeable result of the accident, although the extent of the injury need not be foreseeable’.²⁸ Factual causation requires a showing ‘that the injury would not have occurred “but for” the accident’ or to show ‘that the accident materially contributed to the injury’.²⁹ Unlike Russia, if the plaintiff can establish either but-for or material contribution, the plaintiff can recover regardless of whether something else also contributed to its damages.³⁰ But where the injuries are legally caused by more than one person, the damages will be apportioned among the wrongdoers.³¹

Under English contract law, the ‘but-for’ causation test likewise requires a plaintiff to prove factual causation. The primary goal is to put the plaintiff in the same position he or she was in pre-breach, but to avoid compensating the plaintiff for damages that he or she would have experienced regardless of the breach.³² ‘Legal causation’ is also required under English law. In English law, the concept holds that ‘even though some losses were factually caused by

22 Daria Ilyina, ‘Contracts, Negotiation, and Enforcement in the Russian Federation: Overview,’ *Practical Law Country Q&A* (1 February 2017).

23 Leonardo Canabrava, Lucas Spadano, Ana Paula Lages, Luiza Tângari, Bernardo Santos, Bruno Augustin, Thiago Costa Neto and Fernanda Andrade, ‘Contracts, negotiation and enforcement in Brazil: overview,’ *Practical Law Country Q&A* (1 August 2018).

24 *Nat’l Market Share, Inc. v. Sterling Nat. Bank*, 392 F.3d 520, 525 (2d Cir. 2004); *Herrera v. Sante Fe Public Schs.*, 41 F. Supp. 3d 1027, 1142 (D. Mex. 2014); *Cecala v. Newman*, 532 F. Supp. 2d 1118, 1134 (D. Ariz. 2007).

25 e.g., *Nat’l Market Share, Inc.*, 392 F.3d at 525; *MJS & Assocs., LLC v. Master*, 501 S.W.3d 751, 757 (Tex. App. 2016).

26 See, e.g., N.Y. C.P.L.R., Articles 14-16.

27 See, e.g., Hughes, 17 Fla. Jur 2d Damages Sections 7-16; Section 15:6. Completeness, 43B Mass. Prac., Trial Practice Sections 15:3-15:7 (3d ed.).

28 D. Bruce Garrow, Do-Ellen S. Hansen, Meredith L. Parkes, ‘Damages for Personal Injury or Wrongful Death in Canada’, 69 *J. Air L. & Com.* 233, 237 (2004).

29 id.

30 id.

31 id. at 238.

32 Adam Kramer, ‘Damages for Breach of Contract: An Overview’, 10, *Practical Law UK* (2018).

the breach (that is, but for the breach they would not have occurred), they are nevertheless treated legally as not having been caused by the breach'.³³ Considerations such as foreseeability and remoteness will likely play a role in English courts' common-sense evaluations of whether the legal chain of causation has been interrupted.³⁴

ii Mitigation

Another common principle regarding entitlement to damages is the concept of mitigation, a variation of which appears to exist in most jurisdictions at least in some areas of law. The Russian Civil Code 'allows a judge to reduce the scope of damages if the aggrieved party, intentionally or not, increased the amount of damages or failed to take reasonable measures to reduce it'.³⁵ English courts similarly recognise the concept of mitigation, though if the defendant seeks to reduce his or her damages on the ground that the plaintiff failed to mitigate his or her damages, the defendant bears the burden of providing as much.³⁶ The same is true in South Africa.³⁷

Singapore law requires that, at least in the context of breach of contract, an innocent party act reasonably to mitigate his or her losses, though what exactly qualifies as reasonable is 'often a difficult concept to pin down'.³⁸ In Brazil, though the concept of mitigation of damages has roots in common law, it has been gaining more recognition over the past few decades.³⁹

IV CONCLUSION

The general principles underlying compensatory damages do not vary greatly across modernised legal systems around the world. Actual awards of compensatory damages are therefore driven by the facts of each case and the nuances of the local jurisdiction's governing law. As a best practice, one should partner with a practitioner knowledgeable of the local jurisdiction's practices, rules and precedents to obtain the best result for clients.

33 id. at 12.

34 id. at 12-13.

35 Clare Connellan, Elizabeth Oger-Gross and Angélica André, 'Compensatory Damages Principles in Civil- and Common-Law Jurisdictions – Requirements, Underlying Principles and Limits', *Global Arbitration Review, Guide to Damages in International Arbitration* (2nd edition).

36 Adam Kramer, 'Damages for Breach of Contract: An Overview', 14, *Practical Law UK* (2018).

37 *Cirano Invs. 307 (PTY) Ltd. v. Execujet Aviation (PTY) Ltd.*, Case No. 10831/12 (High Court of South Africa March 22, 2014), www.saflii.org/za/cases/ZAGPJHC/2014/182.pdf.

38 Ian Teo, Kendall Tan, Court Of Appeal Rules On What Constitutes Reasonable Mitigation of Losses (August 2010), <https://eoasis.rajahtann.com/eOASIS/lu/pdf/2010-08-Reasonable-Mitigation-losses.pdf>.

39 R. Coeli Soares Oliveira Veloso, N. Gurgel Vierira: 'Duty to mitigate loss : a Brazilian perspective', *Revue libre de Droit*, 14-26 (2018) www.revue-libre-de-droit.fr/articles/duty%20to%20mitigate%20loss%20a%20brazilian%20perspective.pdf.

RULES GOVERNING EXPERT EVIDENCE ON DAMAGES

*Erik Arnold*¹

I INTRODUCTION

In a court of law, opinion evidence is generally considered inadmissible. Expert opinion evidence is a special exception to this rule and is introduced in court proceedings when specialised or technical knowledge is required to assist the trier of fact in ruling on matters beyond the common knowledge of the court.

In our adversarial litigation system, expert evidence has long been viewed by stakeholders with some apprehension. Experts occupy a grey area between fact evidence and judicial interpretation – the expert’s findings are not strictly factual, but based on opinions, and are therefore subject to the frailties of human nature. Nonetheless, expert evidence plays an important and necessary role in civil litigation. As the complexity of litigation has increased over the years, so too has the role of the expert, expanding to include a broad range of professionals such as accountants, business valuers, forensic investigators, economists, statisticians, scientists and medical professionals, to name a few.

This chapter provides a general framework for the role of the expert in civil litigation, with a particular focus on damages. We first examine the rules governing the conduct of experts. We then examine the content and form of the expert’s report. Finally, we discuss common misgivings that stakeholders have expressed with respect to how expert evidence is tendered in litigation and emerging practices concerning the use of expert evidence at trial.

II RULES GOVERNING THE ROLE OF EXPERTS

i Admissibility of expert evidence and the court’s role as gatekeeper

Expert evidence is allowed only with permission of the court and trial judges remain vigilant in their role as gatekeepers. The courts must weigh the credibility and probative value of the expert’s evidence on a case-by-case basis, routing out faulty or incorrect opinions and excluding entirely those experts who are wholly unqualified or seek to provide opinions outside their area of expertise.

While the case law in different jurisdictions varies slightly, expert evidence is generally considered admissible when the following conditions are met:

- a* the expert’s opinion is relevant to the specific facts at issue in the litigation;
- b* the expert’s opinion is required to assist the trier of fact in ruling on matters that require specialised technical knowledge; and

¹ Erik Arnold is a director at Duff & Phelps.

- c the individual proffered as an expert is properly qualified. This requires that the expert have the relevant knowledge, skill, experience, training and education. The expert's analysis should rely on sufficient facts and data and be premised on sound principles and methods.

Experts are commonly retained to opine on issues relating to the quantification of damages and the courts generally recognise the necessity for independent experts in nearly all cases where a claim for damages is made or where financial analysis is required.

ii The expert's duty to the court

The natural tension between experts and the parties that retain them is a seemingly unavoidable consequence of litigation. The expert is at first recruited (and paid) by advocates, and then asked to provide independent assistance to the courts. In large part to mitigate against the risk of so-called 'hired gun' experts, recent amendments to the rules of civil procedure in many jurisdictions have sought two common objectives – placing clear limits on the allowable scope of an expert's evidence and codifying the expert's overriding duty to the court.

Independent experts are retained, above all else, to assist the court on matters within their expertise and this overrides any obligation to the parties that have retained them. While expectations for experts with respect to independence and objectivity are not new, the courts are shining a brighter light on this issue, developing formal codes of conduct that clearly define the expert's role and restrict improper behaviour. In many jurisdictions, experts must now sign a declaration acknowledging that they have read and understand the rules, agree to be bound by an expert code of conduct and accept their overriding duty to assist the court. This declaration is often appended to the expert's report.

III THE EXPERT'S REPORT

The objective of the expert's report is to effectively and credibly communicate the facts, assumptions and analysis underlying the expert's opinion. Combined with the expert's evidence at trial, including responses to cross-examination by opposing counsel, the report must assist the trier of fact in assessing the merits of the expert's opinion.

While the rules of civil procedure in most jurisdictions provide a general framework for the content of an expert's report, the courts have generally recognised that the specific requirements of an expert's report will vary based on the nature of the analysis and circumstances of each case. The form of an expert's report is also determined, in large part, by the expert's accrediting body, and the practice standards and disclosure requirements governing its members.

In this section we examine the general form and content of the expert's report. While this is by no means an exhaustive list, it highlights some of the critical elements of an effective expert damages report.

i The expert's qualifications and experience

There is a basic requirement for the report to outline the expert's qualifications in the matter at hand so that the expert can be probed by opposing litigants, and the expert's credibility ultimately assessed by the trier of fact. The report should give sufficient details of the expert's

qualifications and relevant professional experience. This requirement is often satisfied by appending the author's curriculum vitae directly to the report. It may also be constructive to provide a list of relevant cases in which the expert has testified.

ii Independence and objectivity

Concern over the independence and objectivity of experts, in fact and appearance, continues to be a major focus for stakeholders in litigation. Regardless of which party has retained the damages expert, the report should include a statement that the expert has acted independently and objectively, and that the expert's compensation is not contingent on the views or opinions expressed therein. In most jurisdictions, the rules of civil procedure require that all experts explicitly acknowledge their overriding duty to assist the court regardless of who is paying their fees, a point emphasised in certain jurisdictions where the report is to be addressed directly to the court and not to retaining counsel.

iii Instructions and assumptions

The expert's report should disclose all of the assumptions underlying the damages analysis, distinguishing between those assumptions that are within the expert's area of expertise (and based on the expert's scope of work) and those that the expert was instructed to take. While the courts recognise that disagreements between experts may result from genuine differences in professional opinion, differences often arise simply from the instructions and assumptions provided by retaining counsel.

The report should disclose the procedures followed by the expert to determine the reasonableness and appropriateness of key assumptions. The expert would typically not be expected to apply the same rigour to given assumptions that fall outside of the expert's area of expertise. These assumptions may include facts in dispute between the parties that will be proven (or disproven) at trial or inputs to the damages analysis provided by other parties. In any event, it is important for the expert to obtain clear instructions from the party requesting the report and, to the extent possible, to assist the trier of fact in differentiating between genuine differences of professional opinion and differences arising from instructions or given assumptions.

iv Scope of review

The expert's report should disclose all material information that was reviewed and relied upon in reaching its conclusion. The expert's scope of review in a damages analysis may include, but is not necessarily limited to, agreements, contracts, financial statements, accounting records, inputs from other subject-matter experts and information available in the public domain, as well as correspondence and interviews with relevant parties. It is the expert's responsibility to gather sufficient documentary evidence to ensure that the conclusions contained within the report are properly supported. When access to essential information is denied by retaining counsel or is otherwise unavailable, the expert should consider whether a qualification to the opinion is required owing to limitations imposed on the expert's scope of review.

The rules of civil procedure in most jurisdictions do not provide much in the way of specific requirements for the expert's scope of review. As a result, exposing deficiencies in the expert's scope of work is often left to opposing counsel and the ultimate assessment is made

by the trier of fact on a case-by-case basis. The thoroughness of the expert's due diligence and scope of work speaks to credibility and is often cited by the courts as a factor in determining the weight placed on expert opinion evidence.

v Calculations and the damages model

The expert's report should provide sufficient information to allow the reader to understand how the expert arrived at the conclusion. A set of schedules is often appended to the expert's report setting out summaries of important financial documents and the calculations supporting the expert's findings.

Given the heightened complexity of modern business decision-making, the scope of accounting systems and the scale of financial record-keeping for most organisations has grown immensely in recent years. The damages expert is often faced with vast amounts of financial data. As the financial information underpinning the analysis grows in complexity, so too does the damages model, which is often required to accommodate many dynamic inputs and alternative scenarios. While an expert's schedules cannot be expected to reproduce every single calculation underlying a complex damages model, the report should sufficiently document the key mechanics, assumptions and data underlying the analysis to assuage any concern that the damages model acts as a 'black box'.

It may be constructive for the expert to produce an electronic version of the damages model. Together with the expert's report and schedules, this allows another qualified individual to verify the accuracy of the model and to reproduce the results using the same data, inputs and assumptions.

vi Working papers

The expert's files should be maintained in an organised manner and the scope of work performed by the expert should be documented. The extent of working paper documentation is largely left to the expert's discretion. As a rule of thumb, the expert's files should retain copies of:

- a* all relevant information relating to the dispute and the specific events giving rise to the claims, including documents and other information produced during the course of the litigation;
- b* any information reviewed, or analysis prepared to provide the damages expert with a background understanding of the subject matter and the broader economic or industry context, including industry research, analyst reports, macro-economic data, metrics for comparable public companies traded on public stock exchanges and other statistics available in the public domain; and
- c* all working papers, data and records underlying the damages calculation itself, including models, calculations, projections, statistics, accounting data, financial statements, forecasts, tax returns and management reports.

Counsel and experts communicate regularly and often by email. The courts have generally recognised that consultation between counsel and experts during the course of preparing a damages report is necessary, within reason, to ensure that all relevant issues are adequately addressed in the expert's report and to facilitate a more timely and affordable process.

Whether and to what extent solicitor–client privilege extends to communications with experts remains a live issue in many jurisdictions, particularly so when experts produce several working drafts of their report, some of which may be reviewed by counsel. The expert should

clearly mark all work-product that is in the process of being completed as being in draft form and subject to change, specifying that the work-product is being issued strictly for the purpose of obtaining comment, instruction or confirmation of facts required to complete the report. While the courts in most jurisdictions increasingly acknowledge that the draft report review process is an important and necessary step in the expert's scope of work, it would be prudent for the expert to document significant changes to the analysis as the draft report evolves, including new facts, assumptions or findings that result in meaningful changes to the conclusion.

vii Limitations and qualifications

A damages analysis is only credible, and ultimately of probative value to the court, if the information underpinning the expert's findings is accurate and complete. It is critical that users of the expert's report understand the nature of the information that was relied upon and any inherent limitations in the scope of the expert's work. As noted earlier, the expert should consider a qualification to their opinion if access to essential information is limited for any reason.

An expert report in a damages case typically includes an overriding assumption that the financial information provided to the expert is accurate and complete. The report should disclose whether or not the expert has audited, reviewed or otherwise undertaken any procedures to determine the veracity of the information relied upon in arriving at the conclusion.

The expert's opinion is a function of the facts and information available at a particular point in time. The expert may reserve the right to modify the report or reconsider the conclusions therein should any new material information or facts be brought to light after the date of the report.

IV ALTERNATIVE APPROACHES TO EXPERT EVIDENCE

Concerns over the cost of litigation are not new. The use of expert evidence in civil litigation and the procedural complications that come along with it are seen by many as contributing, in part, to the rising cost and complexity of litigation. There is also no shortage of cases in nearly every jurisdiction where so-called 'advocacy by experts' has led to a significant miscarriage of justice. For these reasons, the role of the damages expert in civil litigation and the manner in which expert opinions are entered into evidence are evolving. The rules of civil procedure in many jurisdictions are being revised and expanded to permit (or encourage) a number of unique alternatives to the traditional use of expert evidence at trial.

i The traditional approach to expert evidence

In the traditional model to expert evidence, each party to the litigation typically retains their own expert. The experts are asked to prepare their own analysis, commonly exchanging reports and a formal reply report prior to trial. At trial, the qualifications of each expert are first assessed by the courts. If admitted, the experts are then, in turn, examined by retaining counsel and cross-examined by opposing counsel. The experts generally do not communicate directly with one another and comments on the opposing expert's assumptions, methods and findings are limited to the reply report.

ii Jointly appointed experts

The first alternative we will examine is the use of a single, jointly appointed expert. Rules of civil procedure in several jurisdictions now allow for the appointment of a single expert witness to opine on issues in dispute between the parties, including the quantification of damages. The courts have been given increasing latitude to appoint joint experts, showing a particular interest in doing so when the expert is asked to opine on comparatively less controversial quantum issues. The expert may be instructed by the parties or by the court.

In certain circumstances, the use of a jointly appointed expert has been credited with reducing the time and cost of litigation, while also mitigating, in fact or appearance, the ‘hired gun’ mentality of experts. The use of a jointly appointed expert tends to provide a narrow path to resolution on relatively straightforward quantum issues. Settlements are also fast-tracked, perhaps becoming more tenable for litigants when the ultimate outcome on quantum issues is more predictable.

Critics argue that the simple existence of opposing views on a subject are not always indicative of expert bias. Genuine differences of professional opinion may exist within the expert’s field. The appointment of a single expert therefore presumes that the view of a particular expert is correct among a field of others. It can be argued that the use of a single expert therefore inhibits a party’s ability to sample the range of opinions necessary to advance its case.

While the practice of jointly appointed can reduce the cost to litigate relatively simple cases, in more complex litigation the use of a single expert does not necessarily eliminate the need for each party to retain their own subject-matter expertise. These ‘shadow’ experts often assist behind the scenes in reviewing the jointly appointed expert’s report and in identifying avenues for cross-examination. In these cases, the joint retainer may in fact contribute an additional cost burden.

The success of a jointly appointed expert depends, in large part, on having a clear set of instructions that have been agreed to in advance by all parties. Where the court will instruct the expert directly, the marching orders are normally clear. Where the litigants are responsible for jointly instructing the expert, the process can fall apart quickly if proper ground rules are not established from the outset. The ground rules should include clear instructions for timing of key milestones and final deliverables, communication between litigants and the expert, the process for discovery of relevant information and the draft report review process.

The expert should be given latitude to execute the fact-finding and due diligence process in any manner he or she considers reasonable to satisfy his or her obligation to the court and to execute on the scope of work required to support his or her opinion. The expert should be given final say because it is, after all, his or her conclusion being sought and his or her professional reputation on the line when that conclusion is ultimately reported to the court.

The success of a jointly appointed expert depends in large part on fair and open communication between all parties. Any communication to the expert and all information underpinning the expert’s scope of review should be shared among all parties. The need for open communication becomes increasingly important in situations where there is information asymmetry between the parties. For example, in cases where only one party has readily available access to a business’ financial records and documentation, the expert must take care to provide the less-informed party with an opportunity to review and provide context for any information proffered by the other party. Failure to do so will ensure that the expert is only given one side of the story.

The jointly appointed expert can be an efficient and cost-effective method for the court to resolve relatively straightforward disputes, but the use of one requires careful planning and it is important for all parties to respect the process.

iii Concurrent evidence

Another alternative being explored in many jurisdictions is concurrent evidence. Concurrent evidence is at first similar to the traditional approach to introducing expert evidence at trial. Opposing experts are first asked to prepare and exchange their own reports. Questioning at trial then proceeds on familiar terms for each expert – direct examination, cross-examination and reply. In a twist to the traditional model, the experts are then asked to return to the witness box and are questioned together. The necessity for experts to share close quarters during this session gives us the colloquial term ‘hot tubbing’. The hot-tubbing session is typically moderated by the trial judge and questions can be asked by counsel, the court, or both. When it comes to the hot-tubbing session, there are no hard and fast rules.

The experts are often encouraged by the trial judge to reach agreement, where feasible, on issues in dispute. The discussion quickly reveals the critical points on which a party’s case will succeed or fail. If managed effectively, the discussion should clearly identify genuine differences of professional opinion, which are addressed by the experts in real time. The trial judge is given latitude to ask questions of the experts at any time to clarify the courts understanding of key issues. In theory, agreement is reached quicker in a hot-tubbing session because the experts acknowledge that unreasonable assumptions or untenable positions will immediately be exposed by the accompanying expert. The concurrent evidence model puts experts together to address differences in real time, whereas the traditional model could see experts examined days or weeks apart.

The trial judge must play a more active role in the hot-tubbing session. The process is less structured than the traditional counsel-led examination model and the judge must take care to moderate the discussion appropriately prevent the experts from being side-tracked by minor issues and to ensure that the discussion advances towards the genuine and meaningful areas of difference.

A recurring complaint from stakeholders is that the hot-tubbing format tends to favour those experts who are more confident or persuasive in their testimony and there is the risk that assertive personalities will ‘steam roll’ the discussion on critical issues. The trial judge can, to a large extent, overcome this deficiency by way of appropriate moderation of the discussion and probing of the experts.

Counsel is often hesitant to cede control of the proceedings. The real-time interaction between the experts and the direct involvement of the trial judge means the discussion is more fluid and considerably less controlled than counsel’s traditional question and answer examination format.

While there are some practical complications, the hot-tubbing approach is generally seen as an advantageous means of changing the mindset of experts and, under the right circumstances, a valuable tool for the courts to fast track the discussion of otherwise complex issues towards genuine areas of disagreement.

iv Expert witness conferences

We have discussed two alternative approaches to the traditional model of expert evidence – concurrent evidence and jointly appointed experts. A third approach – expert conferences – is viewed as a sort of hybrid of the two.

The concept of expert conferences is fairly simple. Experts retained by opposing litigants meet in advance of trial to exchange information, discuss their findings and identify the significant areas of disagreement. The overriding objective of the expert conference is to narrow the focus of trial to only the genuinely disputed issues.

If so instructed, the experts may draft a joint statement summarising the major areas of agreement and disagreement. This joint statement is then served to the court to assist in better understanding the areas of dispute between the experts, the basis for these differences and the significant 'levers' on which a party's claim for damages will rise or fall. An effective joint statement will also set out the areas of disagreement that are inconsequential to the calculation of damages, allowing the court to set aside these issues and to minimise time spent at trial pursuing any red herrings.

The expert conference must be undertaken in good faith. While counsel may be apprehensive over relinquishing control, it would be improper for an expert to be given, or to accept, instructions not to reach agreement. Experts must approach the conference with a genuine interest in reaching consensus on issues of common professional understanding and identifying errors and omissions in each other's work. Experts may need to abandon positions that do not stand up to the rigours of professional scrutiny or where the underlying analysis is not credible.

The joint statement should provide the court with a clear understanding of the major areas of disagreement and the basis for each expert's opinion. The joint statement should delineate between differences of professional opinion which are within the experts' areas of expertise and differences that result from instructions provided by counsel. Experts should seek further instruction where there are discrepancies in significant facts of the case. Counsel should not be directly involved in drafting the joint statement, although it is not uncommon for counsel for both parties to review a draft of the statement prior to its release.

Preparation is key. If an expert is ill-prepared, the opposing expert's opinions are unlikely to be properly scrutinised and, rightly or wrongly, will dictate the direction of the joint statement. The expert conference should take place at a stage of the proceedings where the important facts of the case are known, typically after production of relevant documents and discovery of key fact witnesses for both parties. It is more effective to hold the expert conference after the experts have issued their reports, ensuring that the position of each expert is on the record prior to meeting.

There has been general support for expert conferences in most jurisdictions, which are commonly ordered by the court prior to, or in conjunction with, the pretrial conference. Expert conferences are now more commonly being used in damages cases to address widespread concerns over the time and cost of litigation. The courts in several jurisdictions have noted widespread support for the practice where expert conferences are already the usual practice. Expert conferences can be particularly effective in damages cases where seemingly vast differences between complex models for calculation damages can often be attributed to a relatively small number of critical assumptions or instructions. The joint statement is an effective method for bringing these differences to light.

V CONCLUSION

Expert evidence will continue to be a necessary and vital part of civil litigation. The courts recognise the importance of the independent expert's report and testimony in nearly all cases requiring the quantification of damages, providing the expert clearly demonstrates an understanding of his or her overriding duty to assist the court above all else. While the courts are yet to find the panacea for all issues plaguing expert evidence, several alternative approaches have emerged that are a step in the right direction towards the delivery of fair, timely and cost-effective access to justice.

CONCEPTS IN FINANCIAL ACCOUNTING AND REPORTING

*Errol Soriano*¹

I INTRODUCTION

Financial damages analyses calculate the difference between the financial results that ‘would have’ occurred absent the actionable event, and what actually transpired.² The assessment of the financial performance of an operating entity includes an examination of the entity’s historical operating results as recorded in its accounting records and reported on its financial statements.

For entities with stable operations, past financial results are often a good predictor of the ‘but-for’ results that the entity would have realised absent the event. In such circumstances, the analyst inherently assumes that the entity’s past, pre-event financial performance would have continued, absent the event. Some minor adjustments to the pre-event results may be required to reflect changes in circumstances, but often these changes are exiguous.

In other circumstances, pre-event financial results are a poor proxy for the but-for scenario. However, this does not mean that the past results are irrelevant. Projecting what would have occurred in the but-for scenario still requires an understanding of how the entity’s revenues and costs vary as production or sales volumes change, commonly referred to as cost-volume-profit analysis. Deconstructing past financial results often uncovers important relationships between revenues, costs and volumes, which is information that underpins the analyst’s but-for financial projection.

Analysis of accounting records also informs the analyst’s assessment of the entity’s actual financial performance and position after the event.

Those involved in assessing financial damages should be interested in the accounting concepts, rules and practices underpinning the preparation of accounting records and financial statements because understanding the accounting framework provides important insight into what the data shows and also speaks to its inherent limitations. From an evidentiary standpoint, accounting records and financial statements are contemporaneous business records that often provide detailed explanations of past transactions and financial events, information critical to proving the financial effect of the event. One cannot evaluate the nature and purpose of past transactions without first understanding the rules governing how the transactions are documented in the entity’s financial records.

The discipline of financial accounting concerns the rules and practices by which an entity’s transactions are quantified, evaluated and aggregated in its accounting records, with similar transactions being grouped into an ‘account’. Each account is assigned an account

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2 What ‘would have’ occurred is called the ‘but-for scenario’. The actionable event is referred to as the ‘event’.

number, and these accounts reside within the entity's general ledger. Accounts are organised within the general ledger by classification. For example, different fixed-asset accounts (automobiles, computers, furniture, etc.) are grouped together under 'fixed assets' in the general ledger.

An accounting system with a relatively high number of accounts allows one to categorise transactions into more homogenous groups. For example, instead of having just one general ledger account for all automobiles, an entity may have separate accounts for automobiles at the head office, the warehouse and the manufacturing plant.

Periodically, the balances in similar accounts are aggregated and reported as a line item in the entity's financial statements. For example, the balances in all of the automobile accounts would be added together and reported as the line item 'automobiles' on the entity's balance sheet. Financial statements can be prepared for any period, but are most commonly prepared on a monthly, quarterly and annual basis.

Financial statements speak to three attributes of the entity's financial circumstances being:

- a* the financial position of the business at a point in time (on the balance sheet);
- b* the financial results (profit or loss) from operations over a specified period (on the income statement); and
- c* the change in the business' cash position over a specified period (on the cash flow statement).

II INTERNATIONAL FINANCIAL REPORTING STANDARDS

For sophisticated entities, financial accounting is governed by rules that provide a degree of standardisation in how similar transactions are recorded and presented on an entity's financial statements. The International Financial Reporting Standards (IFRS) are a set of accounting standards developed to provide a standard global framework for public companies.³

The IFRS Foundation is a non-profit public interest organisation responsible for developing a global set of high-quality accounting standards. The Foundation's objectives include improving comparability of financial information by enhancing transparency and quality, strengthening accountability by reducing the information gap between investors and business operators, and contributing to economic efficiency by helping investors identify opportunities and risks in business ventures.

IFRS is a principles-based system⁴ with broad guidelines, allowing for the use of the accountant's professional judgement in their application. Professional judgement is required because a single set of standards cannot anticipate every possible nuance or situation. However, increased subjectivity in accounting standards may lead to reduced comparability across entities.

3 The United States permits foreign and SEC registrants to use IFRS standards in their US filings but requires domestic public companies to use US generally accepted accounting principles (US GAAP), set by the Financial Accounting Standards Board.

4 US GAAP is a rule-based framework, with a more specific and detailed set of rules, as opposed to the broader principles in IFRS.

The most common measurement basis in financial statements is the historical cost of the item – the amount expended or received. For example, the historical cost of manufacturing equipment is the cost to acquire the machine; wages payable are recorded at the amount owing at the time the liability is incurred.

In some circumstances other bases are used, including the realisable⁵ value (e.g., to set to market the marketable securities that the entity continues to hold on the balance sheet date) and present value⁶ (e.g., to measure the current value of liabilities associated with future pension obligations).

III FUNDAMENTAL QUALITATIVE CHARACTERISTICS OF FINANCIAL REPORTING AND ACCOUNTING

i Faithful representation

It is a fundamental tenet of IFRS that financial information should represent the relevant economic phenomena in a manner that is complete, neutral and free from error.

A complete depiction of a phenomena includes all the information necessary for the user to understand the phenomena.

A neutral depiction means that the basis of reporting is free from bias in selection and presentation. This includes ensuring that phenomena are not discounted, or afforded undue emphasis.

Free from error means that there are no errors or omissions. It does not mean accuracy in all respects. For example, a bad debt expense is management's estimate of the proportion of accounts receivable that are likely uncollectible at a given point in time. This estimate is a faithful depiction if the amount is clearly described as an estimate and that the estimate has limitations.

ii Relevance

Accounting standards are designed to provide relevant information to the users. Relevant information can make a difference in the users' decisions, whether or not they take advantage of it.

Relevant information can have predictive value, confirmatory value or both. Data has predictive value if it is relevant to forecasting financial performance, and confirmatory data is used to confirm or amend previously held views and conclusions.

In a damages analysis, historical financial statements are relevant in both respects. The information is often predictive, and is thus used as a starting point to project future financial performance (absent the event). The data in financial statements can also be confirmatory to the extent that it speaks to the financial effect that the event has had on the financial performance or position of the entity.

5 Assets are carried at the selling price and liabilities are carried at the undiscounted amount expected to be paid.

6 Assets and liabilities are carried at the discounted future cash inflows (outflows) generated (realised) under the normal course of business.

That said, an entity's accounting and financial reporting systems are set up to fulfil statutory reporting requirements and provide management with key operational information; the systems are not often specifically designed to accommodate what can be the somewhat unique information requirements in an exercise to prove financial loss.

This limitation on the usefulness of accounting systems in the context of proving financial loss has been ameliorated in recent years as modern accounting systems store data in relational databases, and these systems are capable of aggregating transactional data in a customised format that is responsive to the somewhat unique needs of the damages expert.⁷

However, even with these technological advances the accounting and reporting systems are but one source of relevant information concerning the affairs of the business. For example, the state of the entity's relationships with its customers, suppliers, lenders and employees, or management's expectations for the future will not be evident in financial statements and the general ledger alone. Thus, the analyst must examine other relevant financial information, such as contracts, agreements, financial forecasts and industry information, among other things.

iii Understandability

The challenge in financial reporting is to distil a large volume of what are often complex transactions into a relatively brief, understandable format. The premise underlying IFRS is that the user has a reasonable knowledge of the business and that the user will review the financial statements diligently.

Given the natural tension between the competing objectives of relevance and understandability, financial statements cannot be all things to all users – certain users may need to seek additional information from other sources (including the accounting records underpinning the financial statements), and the assistance of financial and accounting experts.

For example, if the analysis involves valuing the shares of the business, the analyst will examine the data reported in the financial statements, but this information is often at too high a level to complete the picture. For example, management salaries are an expense amount reported in aggregate on the financial statements that is often examined in greater detail to determine which costs are required to operate the business as opposed to amounts incurred for tax planning or other purposes. The financial statements commonly report total salaries expense as a line item on the income statement, but not who was paid what during the year. For that level of detail, the analyst must refer to the source accounting records, including payroll records and general ledger account detail.

iv Materiality

Information is material for financial reporting purposes if its omission or misstatement on the financial statements could influence the user's evaluations or decisions. The determination of what constitutes a material item is largely a matter of professional judgement. For example, a US\$100,000 misstatement in a small business may be material, but may not be for a large multinational entity.

⁷ A relational database comprises multiple data sets organised by tables with different tables storing different categories of information, each linked to the other tables with one or more common data fields. Functionality within the system allows data to be extracted and aggregated from different tables, which facilitates data searchability, analysis, organisation and reporting.

In a damages analysis, the threshold of materiality is often much lower than the level governing the preparation of the entity's financial statements. As such, the analyst will often examine the underlying accounting records, which have more detailed and disaggregated information (that is not material to present on the financial statements).

v Comparability

Comparability refers to the consistency of an entity's results across time periods and is enhanced when similar events and transactions are treated consistently in the entity's accounting records. Comparability also refers to the ability to benchmark results among different reporting entities.

There is a natural tension between relevance and comparability; more rigid accounting rules may result in a one-size-fits-all approach in reporting what can be a somewhat heterogeneous set of transactions. Broader guidelines that leave more to the accountant's judgement may provide the flexibility needed to better capture the essence of the transactions (enhancing relevance), but these judgements are subjective, possibly leading to variances in accounting treatments and reducing comparability.

vi Timeliness and cost

Timeliness and costs are constraints to financial reporting. In regard to timeliness, information is only relevant to the extent it is available to the decision makers before they have made their decision. The longer one takes to prepare the financial statements, the less relevant that information is to the decision maker, even if the interim time is spent gathering more precise data. Similarly, the cost of producing additional analysis may outweigh the value and materiality to the user.

IV ELEMENTS OF THE FINANCIAL STATEMENTS

The five elements of financial statements are assets, liabilities, equity, revenues and expenses.

An item that meets the definition of an element should be recognised if:

- a* it is probable that any future economic benefit associated with the item will flow to or from the entity; and
- b* the item has a cost or value that can be measured with reliability.⁸

The financial statements also include notes, which provide further information on amounts reported in the financial statements and other issues affecting the business.

In some circumstances, where an item is not recognised in the financial statements, note disclosure is included. Note that the amount of the potential benefit or cost need not be certain to be reported.

⁸ The Conceptual Framework for Financial Reporting, IFRS.

i The balance sheet

The financial position of an entity at a specific point in time is reported on its balance sheet, which separately lists the entity's assets⁹ and liabilities,¹⁰ the net of which is the entity's equity position.

ii Assets

Assets are reported (on the balance sheet) when the cost can be reliably measured, and it is probable that future economic benefit will flow to the entity.

Economic benefits include items that furnish capacity to produce goods or services (e.g., equipment), items that can be exchanged for other assets held by another entity (e.g., inventory) and items that can be used to settle a liability or can be distributed to the owners of the entity (e.g., cash and marketable securities).

Many long-term assets are depreciated across their useful lives, under a systematic process where an expense is recorded and the asset's carrying amount is reduced each period by that same expense amount.

It is noteworthy that the entity need not own the item to expect to receive future economic benefit. For example, a leased item may be classified as an asset because the entity will realise long-term future economic benefits from the lease, even though the entity does not own the underlying leased item.

Assets can be classified as tangible or intangible.¹¹ For example, manufacturing equipment is a tangible asset, as its economic benefits derive from its physical properties. In contrast, a patent is an intangible asset because the value of the asset comes not from the physical legal document evidencing the patent, but rather from the legal rights of the patent.

Assets are periodically tested for impairment, and the value is written down if the future benefits are lower than the carrying value. While such analyses can be useful information in the context of a damages analysis, it is important to appreciate that the carrying value of assets on financial statements are set in the context of financial reporting, not in the context of litigation, and often more detailed analyses is required to prove financial loss.

iii Liabilities

Liabilities are the present obligations of the entity. In this context, the obligation is a duty or responsibility to act or perform in a specific way. For example, accounts payable arise when the entity has received goods or services and has undertaken to pay for those goods and services at some point after delivery. Some obligations are legally enforceable by contract (e.g., loans) or statute (e.g., taxes payable). In other cases, an obligation may arise from voluntary business decisions. For example, if an entity decides to rectify a complaint even though not legally required to do so, the total future cost of rectification may meet the liability test.

9 A resource controlled by the entity as a result of past events from which future economic benefits are expected.

10 Present obligation from past events, the settlement of which is expected to be an outflow of resources.

11 Intangible assets are non-physical assets where the benefit to the business comes from the rights and/or privileges inuring to the owner. Tangible assets have a physical substance.

Liabilities are recognised when the cost of the liability can be reliably quantified. Where this is not the case (e.g., when the outcome of a pending lawsuit is uncertain), the entity may still be required to provide information concerning the obligation in the notes to the financial statements.

iv Equity

Equity is the difference between the reported values of the entity's assets and liabilities. It is the residual interest attributable to the owner of the entity. Note that this 'value' to the shareholders reflects valuation rules applied in the context of financial reporting; in most cases the fair market value of the shareholder's equity will be different.

Equity can be broadly organised into two categories: (1) amounts contributed by the owners of the entity; and (2) retained earnings, being the cumulative net income that the entity has earned in the current and past reporting periods that has not yet been distributed to the owners.

v The income statement

The entity's financial performance (i.e., profit) is measured as the difference between its income and the expenses it incurs to earn the income. The net result is the entity's net income (or loss) for the period and this is reported on the entity's income statement.

vi Income

Income is the economic benefits flowing to the entity in the form of cash or enhancements to its assets, or reductions to its liabilities. Income includes benefits derived from normal operations (the sale of goods or the rendering of services) and amounts from unusual or non-recurring activities such as the gain on the sale of manufacturing equipment (where proceeds exceed the carrying cost of the item). For the purposes of financial reporting, it is often the case that income from core activities and unusual and non-recurring income amounts are segregated on the income statement so that the user can more easily evaluate the results from the entity's core operations.

vii Expenses

Expenses are the outflows of economic benefits from the business that the entity undertakes in the expectation that the outflow will provide resources, such as goods, services or efficiencies to the business in furtherance of its objective of earning income.

The matching principle is an axiom of financial reporting, stating that expenses are to be reported in the fiscal period in which the economic effect from the expenditure is realised.

In many circumstances matching the expenditure and economic effect from the expenditure is simple. For example, wages are paid in return for services rendered by employees, and for most of the year the cost and economic benefit are realised in the same fiscal year. However, consider the circumstance at year-end (say 31 December); employees have provided services in the last two weeks of December and are paid for these services in January of the following year. If one were to record the expense when the wages were paid (in January of the following year), there would be a mismatch between the year in which the economic benefit was received and the year in which the expense was recorded in the financial statements.

Accrual accounting is a process used to effect the matching principle, under which expenditure is accrued, to reallocate the expense from the period of the payment to the period in which the economic effect from the expenditure was realised. In the example above, the wages expense is reallocated from January to the previous December.

Another common example of accrual accounting involves the accounting treatment for capital assets, such as manufacturing equipment. While the expenditure to acquire the asset occurs in one fiscal year, the economic benefit from the expenditure (provided by the continued use of the equipment over time) is realised over several subsequent years. In this circumstance it would be inaccurate to reflect the entire expenditure to acquire the equipment as an expense in the year of acquisition. Instead, the costs are spread over the economic life of the item, through depreciation expense.

In essence, portions of the capital asset are transferred from an asset (on the balance sheet) to an expense (on the income statements) as the economic life of the asset is consumed over time.

Another category of expenses pertains to unusual and non-recurring non-operating expenses. These amounts often relate to reduced asset values arising when the reported value of an asset has diminished during the year, either due to market forces (e.g., in the case of marketable securities) or as a result of a loss on sale of an asset (i.e., where the proceeds from the sale are less than the carrying value of the item in the entity's accounting records).

It is often the case that expenses from core activities are segregated from the unusual and non-recurring amounts so that the user of the financial information can more easily evaluate the results from the entity's core operations.

viii Cash flow versus net income and the statement of cash flow

Net income, the difference between the entity's income and expenses, is a measure of the profitability of the business. Profit is a useful measure of the long-term viability of the entity. However, cash flow is also vital to the business – an entity can be profitable and yet its ability to operate can still be threatened by a shortage of cash.

This disconnect between accounting profits and cash flow arises, in large part, from the matching principle and accrual method of accounting.

If all of the entity's income and expenses are received and paid in cash, then its net income equals its cash flow. For most entities this is not the case. Consider that income is realised when the benefit has been earned, even if the cash is only received later. For example, a law firm may issue an invoice on day one, and recognise the income on that date, but will only realise the cash inflow on a later date (when the client pays the invoice).

The same holds true for expenditures. Consider the previous example of manufacturing equipment. It is acquired on day one and, because it is expected to contribute economic benefits over several years it is recorded as an asset (typically at the cost to acquire the item). For simplicity, assume that the entity paid cash to acquire the asset. All the cash outflow is realised on day one even though no expense (which reduces net income dollar for dollar) has yet been recorded. Subsequently, the asset value is then reduced in increments to reflect that portion of the economic life of the asset that is consumed in operations each period, and the incremental consumption in any given period is reported as depreciation expense (which reduces net income) – but there is no cash outlay from this event.

The statement of cash flow reports the business' sources and uses of cash over a specified period. Sources and uses of cash arise from the operating results of the business (net income adjusted to reflect changes in non-cash balances during the period); financing activities

(increases in bank financing, repayments of bank financing, or changes in the amount of equity invested in the business); and investment activities (cash expenditures on items such as new investments in plant and equipment).

In terms of assessing financial loss, one examines the income statement, but in many cases the most accurate basis to measure the loss is based on cash flow, and the analyst will adjust the reported profitability to reflect the timing differences between net income and cash flow and then measure the entity's financial loss based on the diminution in cash flow post-event.

V SUMMARY

In the context of quantifying financial loss, financial statements provide important information. However, in most cases, the aggregated data in the financial statements is at too high a level to establish the specific dollar value of a financial loss arising from an event. To isolate the financial effect of an event, the analyst must look behind the financial statements, to the entity's underlying accounting and business records.

OVERVIEW OF THE FINANCIAL DAMAGES MODEL FOR INCOME LOSS

*Errol Soriano*¹

I FRAMEWORK

Quantifying financial loss involves a hypothetical exercise of placing the injured party in the position they would have occupied but for the wrongdoing. In the case of breach of contract, this involves placing the injured party in the position they would have been in had the contract been fulfilled; in the case of tort, the exercise involves placing the party in the position they would have occupied had the tort not occurred.

In most circumstances, the financial loss is based, at least in part, on the diminution in the injured party's revenues from the wrongdoing. However, it is also common that the injured party has experienced increased costs as a result of the wrongdoing and this is typically quantified as a separate head of damages.

The plaintiff bears the burden of proving its loss, and damages are intended to be compensatory, not punitive. 'There are two essential principles in valuing that claim: first, that the plaintiffs have the burden of proving their loss: second, that the defendants being wrongdoers, damages should be liberally assessed but that the object is to compensate the plaintiffs and not punish the defendants.'²

At its highest level, the damages framework calculates the financial loss as the difference between the incremental revenue that the injured party would have realised net of the incremental costs that would have been incurred to realise that incremental revenue.

The analysts' work is governed by common principles and practices of financial analysis together with common law that addresses such issues as the date of assessment, mitigation, remoteness and foreseeability.

However, it is almost always the case that the analyst's professional judgement will play an important role in the assessment. The purpose of this chapter is to set out key components and considerations governing the analyst's work.

II HINDSIGHT

When determining the course of action that the plaintiff would have undertaken in the 'but-for' world, the use of hindsight is not generally permitted. For example, when considering whether the plaintiff would have manufactured and sold the product itself, only the information available to the plaintiff at the time should be considered.

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2 For example, in the context of patent infringement, see *Lord Wilberforce in General Tyre & Rubber Co. v. Firestone Tyre and Rubber Co.* [1975],[1976] R.P.C.197 (U.K. H.L.), which cites *Pneumatic Tyre and Puncture Proof Pneumatic Tyre* (1899), 16 R.P.C. 2019 (C.A).

Having established the injured party's course of action in the but-for world, hindsight is then permitted to determine the monetary value of this but-for scenario. For example, in the case of a patent infringement, the royalty rate that would have been charged is based on a hypothetical negotiation, the assumed terms of which are based only on the information available to the parties at the time the rate was set – without the use of hindsight. However, the product sales revenues (on which the royalties are payable) may be determined with the benefit of hindsight (based on, for example, actual volumes sold during the loss period).

III INCREMENTAL REVENUE

At the core of most damages analyses is the projection of the revenue that the entity would have realised but for the alleged wrongdoing. We say this because the expenses that would be incurred to earn that incremental revenue can usually be determined based on the analyst's assessment of the cause-and-effect relationship between revenues and expenses, commonly referred to as a cost-volume-profit analysis.

Lost revenues can arise from decreased sales volumes, price suppression, or both.

By its nature, projecting lost revenues can be a somewhat subjective exercise because one is hypothesising about the financial performance of the business absent the event.

Past financial performance can be a useful proxy to project the financial performance during the loss period, particularly in circumstances where the industry the entity operates in is stable. But, in most circumstances, the analyst will also have to consider the impact of circumstances existing during the loss period. The analyst will consider industry and economic factors and how they have changed over time, together with the plaintiff's circumstances, including, but not limited to, the plaintiff's efforts at mitigating its losses.

An often-quoted case on mitigation is *British Westinghouse Electric and Manufacturing Co. Ltd v. Underground Electric Railway Co. of London Ltd*, in which the court stated:³

The fundamental basis for the assessment of economic damages is that compensation for pecuniary loss naturally flows from the breach: but this first principle is qualified by a second, which imposes on the plaintiff the duty of taking all responsible steps to mitigate the loss...and bars him from claiming any part of the damage which is due to his neglect to take such steps.

What constitutes reasonable attempts at mitigation is fact specific and while the determination is often based on argument presented by counsel, the financial analyst can play an important role in assessing what constitutes reasonable courses of action from a business risk and cost perspective – important considerations for the court to evaluate in its deliberations.

IV INCREMENTAL EXPENSES

Revenues and expenses exist in a cause-and-effect relationship. Having first assessed the effect that the wrongdoing has had on revenues, the analyst can then turn his or her attention to the expenses that would be incurred to realise those lost revenues. The analyst will typically undertake what is termed a cost-volume-profit analysis that seeks to identify the underlying relationship between revenues, costs and production volumes. Simply stated,

3 [1912] A.C. 673 (H.L.O.).

the analyst examines how costs change at various levels of revenue and production. Having established the relationship between these variables, it is usually straightforward to project the incremental costs that would have been incurred to realise the lost revenues (i.e., absent the alleged wrongdoing).

Costs are commonly categorised by their behaviour and common categories include variable costs, fixed costs, semi-variable costs and step costs.

i Variable costs

Costs are categorised as variable costs if they vary in proportion to changes in revenue or production volume. Common examples of variable costs include sales commissions paid as a percentage of revenue and materials used to produce a product.

Identifying and segregating these costs from other types of costs is important because it provides insight into the profitability of incremental units of production or sales. The difference between revenues and variable costs is termed contribution margin.

ii Fixed costs

Fixed costs are incurred in set periodic amounts that do not fluctuate with changes in production volume or revenues. Stated another way, a fixed cost is incurred at a set amount regardless of whether the company earns US\$1 of revenue or US\$1 million of revenue. Common examples of fixed costs include rent, insurance and C-suite expenditures.

In most circumstances, where the plaintiff's business continues to operate during the loss period despite the alleged wrongdoing, fixed costs are excluded from the analysis of financial loss because these costs would have been incurred regardless of the wrongdoing. In other words, these are not incremental costs incurred to earn the lost incremental revenue.

iii Semi-variable costs

Semi-variable costs are a hybrid between fixed costs and variable costs in that a component of the cost is a fixed periodic amount but other parts of the expenditure are variable with changes in revenues or production. Returning to the above example of the sales commission that was viewed to be a variable cost, it may be the case that a portion of the sales commission is a fixed periodic amount with a second component being based on sales volumes, in which case the expense would be considered semi-variable. Another common example involves utilities where a certain base amount of expenditure is required to keep the lights on, but additional energy may be expended to produce incremental units of the product.

The analyst will examine the nature of these semi-variable costs, and in particular how they behave at different levels of sales or production volume (as the case may be). Having already projected the incremental revenue, the analyst will project the change in the semi-variable cost amount required to earn the incremental revenue, and this amount is deducted from incremental revenues in the financial loss analysis.

iv Step costs

Step costs remain constant for a certain range of production volume or revenues but then change to a new plateau for revenue or production volume outside that range. For example, in a manufacturing facility, wages paid to production line workers on one production line

would be a fixed amount, but if subsequent increases in production necessitate a second production line, the total wage cost will step up to reflect the additional costs paid to employ the second line of workers.

The analyst examines the entity's sales or production capacity and, based on his or her projection of the but-for revenues, projects the incremental step costs that would be incurred (to the extent existing capacity is determined to be insufficient to meet the projected but-for volumes or revenues).

V THE PRESENT VALUE OF FUTURE LOSSES

Future losses refer to the financial loss, arising from the wrongdoing, that will occur after the date of the trial. These losses are projected to the end of the loss period and then discounted back to the trial date using the appropriate 'discount rate'.

One should not read too much into the term 'discounted' – discounting future amounts is based on mathematical formulas, rather than a simple percentage reduction in the future dollar amounts. The formulas are well known and based in large part on the assumed rates of return employed therein.

It is axiomatic that a dollar received today is worth more than a dollar received a year from now because the dollar received today can be invested, earn income and grow to a larger amount by that future date. Furthermore, the risk of realisation of receiving a dollar today is nil whereas there may be some risk of realisation for amounts to be received on future dates.

The concept of present value equates a stream of future payments to a lump sum, which, if handed to the recipient today, would grow at a specified rate of return to exactly equal to future sum on the future date it becomes due. In effect, future loss amounts are 'discounted' to their present value.

Based largely on this premise, awards for future financial loss are discounted to their present value on the date of the award. As noted in the case of *McCarter Burr Co Ltd v. Harris*:⁴

If the choice had been given of accepting half of the sum in ready cash or going on and taking all the uncertain chances of the popularity of a patent medicine continuing, of going on with the business expenses in the way of persistent and costly advertising and of seeking and filling orders and paying salaries to its officers, I feel sure that it, the plaintiff, would have hesitated long before refusing it and would in its consideration of the offer, not have felt as much certainty about its future business as its officers seemed at trial to entertain.

From a damages perspective, the rates of return employed in determining the discount rate should reflect the risk that future loss amounts may not have been realised absent the actionable event. In effect, the discount rate reflects the risk-adjusted after-tax rate of return that an investor would require to be indifferent between receiving the present value of the future loss (i.e., the loss amount) or the right to receive the future loss amounts as they would have come due absent the alleged wrongdoing.

4 (1922), 70 D.L.R. 420 [1922] 3 W.W.R 929, 18 Alta. L.R. 609 (S.C. APP. Div).

The analyst plays a large role in assessing these risks of realisation; the analysis is based in large part on the analyst's assessment of the risks and opportunities in the industry in which the entity operates, the entity's historical financial performance and prospects, as well as those of its peers to the extent that such information is publicly available.

As noted in the case of *Murano v. Bank of Montréal*:

[I]n assessing the reliability of projected future profits, a record of past earnings will obviously increase the certainty of such a prediction. However, a lack of evidence of past earnings does not automatically preclude a new business from recovering for lost profits. Rather, a new business must be allowed to prove lost profits to a reasonable level of certainty by expert testimony, by evidence of actual profits of similar businesses, by evidence of proven managerial experience and expertise, and by evidence of subsequent earnings if such evidence is available. Nevertheless, damages should not be awarded for lost profits which are entirely speculative and uncertain.⁵

The analyst's risk assessment will evaluate the reliability of the financial projections prepared by the analyst or the company, as the case may be. Relevant considerations may include, but are not limited to, the following:

- a* the extent to which the projections were prepared by persons with knowledge of the industry;
- b* the extent to which the plaintiff's financial projections were corroborated by the defendant's own information;
- c* the extent to which the analyst has softened the impact of the projections. The analyst should have good reason before adjusting the financial projections but, if done, the fact remains that by forecasting financial results less than those indicated in the financial projections prepared at the time, the risk that the injured party would not realise the amount forecast in the analyst's report is reduced;
- d* availability of corroborating third-party, arm's-length data, such as industry growth projections prepared by an industry association that corroborates the assumptions and analysis included in the financial projections; and
- e* the scope and rigour of the analyst's analysis to test the reasonableness of the assumptions employed in the financial projections.

VI ASSUMPTIONS

Given that the analyst is tasked with determining the financial effect of the 'but-for' scenario, he or she will necessarily employ assumptions in his or her analysis. In broad terms, assumptions can be segregated into those that pertain to law, those that pertain to facts, and those that are required to frame the analyst's damages model.

Assumptions pertaining to matters of law are outside the expertise of the analyst and, in most cases, such assumptions are provided by counsel. For example, the analyst may be instructed to assume that the terms of a signed contract are binding.

Some assumptions regarding assumed facts will address events. For example, the analyst may be asked to assume that a binding verbal representation was given during a meeting

⁵ 1995, 41 C.P.C. (3d) 143 (Ont. Gen Div).

between the litigants. In most cases these assumptions will be taken as given by the analyst because it would be inappropriate for the analyst to provide commentary and opinion on findings of fact and legal interpretation, which, by their nature, are the purview of the court.

That said, in other circumstances the analyst will be able to assess the reasonableness of these assumptions by, for example, evaluating contemporaneous documents such as emails, agreements and meeting memorandum. For example, the analyst may have been asked to assume a certain volume of lost sales but may be able to establish the veracity of the assumption based on the terms specified in the correspondence between the parties.

The third category of assumptions are those required as parameters for the loss analysis, and in many cases these are developed by the analyst, possibly with some input from counsel. Examples of these types of parameter assumptions include, for example, the period of loss.

VII ACCOUNTING FOR PROFITS

This remedy is most commonly available in two types of cases:

- a* in a breach of fiduciary duty case where a competitor has had illegal access to the entity's trade secrets, customers or other proprietary systems; and
- b* in a case involving the infringement of intellectual property rights.

The objective in an accounting for profits is to require the defendant to disgorge all profits made as a result of the infringement.

i Breach of fiduciary duty

In many jurisdictions it is common that remedies for breach of fiduciary duty are discretionary, and depend all on all the facts before the court. The remedies are designed to address not only fairness between the parties, but also the public concern about the integrity of fiduciary relationships.

Many of these cases revolve around an employee that leaves the business to compete, unfairly, by utilising confidential corporate information or resources to gain a competitive advantage in the marketplace, or by soliciting corporate customers in violation of non-compete agreements or other statutory or contractual obligations.

Although the case law varies by jurisdiction, from a financial perspective the case of *de Florio v. Con Structural Steel Ltd* sets out a common arithmetic process to quantify the ill-gotten profits, as follows.

First, it is necessary to establish the length of the period during which the fiduciaries are obligated not to solicit former clients. Second, the plaintiff has the option to seek either the profits it has lost, or the profits the defendants have gained during the non-solicitation period. Third, the list of former customers successfully solicited during the non-solicitation period must be established. Fourth, the value of the solicited contract must be calculated. Fifth, it is generally appropriate to apply a discount to the calculation of the lost profits. The discount will account not only for the competitive nature of the business in question but will also account for the fact that the plaintiff would not have been guaranteed to receive the disputed contract if the defendant had not been present as a competitor in the marketplace (to the extent this is the case).

The defendant's cost structure will be different from that of the plaintiff, and therefore the profit that the defendant made from the wrongful act will be different from the financial loss suffered by the defendants, and the difference it is often material.

For example, the cost of inputs necessary to provide the services or produce the products may vary depending on the relationships with the suppliers. Also, larger operations have efficiencies (economies of scale, etc.) that can reduce costs of production.

If the process permits, it behoves the plaintiff to assess both available remedies (damages and the accounting for profit) to determine which calculation yields a larger value. However, in some circumstances the plaintiff may be obliged to choose between an accounting of profits and a damages analysis at an early stage in the proceedings, in which case the analyst may provide judgement based on what can admittedly be only a preliminary understanding of the operations of the two businesses.

ii Patent, trademark and copyright infringement

Accounting for profits is also available in the context of patent, copyright and trademark infringement cases. While it is common for statutory provisions to provide authority for an accounting for profits, this remedy is also available as an equitable remedy in many jurisdictions. For example, see *Siddell*.⁶

In an accounting for profits, the inventor is only entitled to that portion of the infringer's profit that is causally attributable to the invention. There has been recent analysis regarding what is meant by the term 'profit' in this context.

Historically, the meaning of profit simply meant the difference between revenues and costs. 'Profit is the difference between expenditures made to produce and sell the infringing articles and the receipts therefrom.'⁷

However, more recently the framework has shifted to a differential approach. In *Monsanto Canada Inc v. Schmeiser*, the Supreme Court of Canada held that the preferred means of calculating profits is the differential profit approach, described as 'a comparison is to be made between the defendant's profit attributable to the invention and his profit had he used the best non-infringing option'.⁸

The practical significance of the difference between the two approaches is shown in *Schmeiser*. The defendant infringed Monsanto's patent by growing genetically modified canola (which rendered it resistant to herbicide). However, the defendant claimed that it had gained no financial benefit from the use of the invention; there was no evidence to show that the defendant took advantage of the herbicide resistance by spraying the herbicide and, because the defendant sold the canola seeds for crushing rather than as seed, the sale price was no higher than it would have been had he planted unpatented seed. The trial judge measured the losses as the difference between the revenues from those crops and the costs incurred to grow the crops (i.e., the historical methodology). Upon appeal, the Supreme Court of Canada used a differential approach and found that the defendant's profits 'were precisely what they would have been had they planted and harvested ordinary canola... The appellant's profits arose solely from qualities of their crops that cannot be attributed to the invention'.⁹

6 *Siddell v. Vickers* (1892), 9 R.P.C. 152 (C.A.).

7 Preston P in *Teledyne*, *infra* note 166 at 110, quoting *Levin Bros. v. Davis Mfg. Co.* 72 F 2d.163 (8th Cir., 1934) at 165.

8 *Monsanto Canada Inc. v. Schmeiser*, 2004 SCC 34, 2004 CarswellNat 1391, 2004 CarswellNat 1392, [2004] 1 S.C.R. 902, 31 C.P.R. (4th) 161 (S.C.C.).

9 *ibid.*

VIII SUMMARY

At its highest level, the quantitative framework underpinning an accounting for profits or damages analysis is well established. The challenge in a particular case is for the analyst to populate the framework with parameter estimates and assumptions that are well-reasoned given the facts of the case, and supported by empirical or corroborating third-party evidence.

THE FINANCIAL DAMAGES MODEL FOR LOSS OF VALUE

*Neil de Gray*¹

I INTRODUCTION

Damages are generally calculated as either (1) a loss of income or (2) a loss of capital. When damages are determined on account of a loss of capital, it is often necessary to perform a valuation of an asset or business.

This chapter is intended to provide an overview of business valuation principles, concepts and methodologies, and to explain how they apply to the calculation of damages. Although the valuation of any particular asset or business will depend on case-specific factors, the general principles outlined herein can be broadly applied. That said, there is no valuation formula or rule and the determination of value is inherently subjective. It is generally advisable that parties engage a qualified business valuation professional where a formal business valuation is required.

II DEFINITION OF FAIR MARKET VALUE

The first step in any valuation process is to clearly understand what exactly is being valued. A valuator may be tasked with valuing a business in its entirety, including both its equity and debt components (enterprise value), specific equity or debt interests in a business, or specific assets of a business. Establishing what is to be valued is a critical first step in the valuation process.

The valuator must also establish the definition of value to be adopted. In general, business valuations typically focus on the determination of 'fair market value'²; however, other definitions of value may be relevant in certain case or fact situations.²

The definition of fair market value varies to some extent by jurisdiction. In the United States, fair market value is defined as:

*The price at which 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.*³

1 Neil de Gray is a director at Duff & Phelps.

2 For example, in Canada, 'fair value' is generally adopted as the definition of value to be used in cases involving shareholder oppression, shareholder dissent and in family law. Fair value is commonly defined as fair market value without the consideration of a minority discount and/or premium for control.

3 *United States v. Cartwright*.

In Canada, the generally accepted definition of fair market value is:

The highest price available in an open and unrestricted market between informed and prudent parties, acting at arm's length and under no compulsion to act, expressed in terms of cash.

Although the definition of 'fair market value' varies to some extent by jurisdiction, the general underlying components of the definition remain consistent.

i Highest price available

Conceptually, a buyer and a vendor will only transact at a price and upon terms to which they both agree based on their own motivations and self-interest. The transaction price is the price at which the vendor's interest, which is to maximise the selling price, and the buyer's interest, which is to minimise the purchase price, are in equilibrium. Fair market value determined in a notional context reflects the highest price available.

ii Willing buyer and willing seller: no compulsion to act

The fair market value definition assumes that the parties are willing participants in the transaction and neither party is forced to transact. In reality, a business owner may be compelled to sell their ownership interest for a variety of reasons including personal health or financial difficulty.

iii Knowledge of relevant facts

The fair market value definition assumes that both the vendor and the purchaser are informed with respect to all material facts important to the value determination and will act prudently.

All information that would or should have been available at the valuation date is assumed to have been available in the notional market value determination. It is generally accepted that hindsight information, information that could only be expected to have been known after the valuation date, is not considered in the fair market value determination.

iv Acting at arm's length

The definition of fair market value assumes that the buyer and seller are arm's-length parties and will negotiate in accordance with their self-interest.

v Open and unrestricted market

Fair market value assumes an open and unrestricted market that includes all potential acquirers. All potential purchasers with the will and resources to transact are included in the valuator's considerations. Any restrictions that may influence the marketability of a business are assumed to be temporarily lifted for the purpose of determining value in a notional context. To the extent restrictions exist, the valuator may consider the impact of the restrictions by applying a reasonable discount to the value that has otherwise been determined.

vi Expressed in terms of cash or cash equivalents

Fair market value is expressed on a cash equivalent basis and assumes the transfer of the rights and risks associated with the business at the valuation date. This is often in contrast to open market transactions, which are frequently consummated based on non-cash consideration, such as the transfer of shares, or involve payments over a period of time (an earn-out).

III OPEN MARKET PRICE VERSUS NOTIONAL FAIR MARKET VALUE

Price and value are two distinct concepts that are often confused in consideration of a valuation.

The price of a business or asset is based on the negotiations of a buyer and seller in an open market transaction and reflects the actual terms of a sale.

Value is generally determined in the context of a notional market, where the enterprise subject to valuation has not actually been exposed to the market for sale. The notional market is intended to replicate what may be expected to occur in a rational, fully informed and liquid marketplace without exposing the business interest for sale.

Notional fair market value is generally determined on an intrinsic (stand-alone) basis without the consideration of the potential synergies or economic benefits that may accrue to a subset of the potential purchasers of a business. Certain purchasers may be willing to pay a price that is different from intrinsic value because of their specific circumstances and the specific benefits they may receive from an acquisition. These purchasers are commonly referred to as special interest purchasers.

Quantifying the premium that a special interest purchaser may be willing to pay for synergies is often difficult in a notional market context as the information necessary for the valuator to accurately assess synergies is generally unavailable. As a result, the price arrived at in an open market transaction may be different from the value conclusion reached in a notional market valuation at the same valuation date.

Notional fair market value may also differ from price because of the following:

- a* Information asymmetry. Open market transactions are negotiated between parties with varying degrees of knowledge and as a result the transaction price may be different from the 'highest price available' as determined in a notional market context.
- b* Compelled parties. A vendor may be compelled to sell their business as a result of personal health, financial or other reasons. Forced open market transactions may result in a price that is lower than notional fair market value.
- c* Non-cash consideration. Open market transactions often involve non-cash consideration or other forms of compensation including earn-outs and employment contracts that impact the price paid.
- d* Imprudent decisions and human emotion. A purchaser or vendor may negotiate an open market transaction based on human emotion that does not reflect the 'highest price available'.

IV VALUATION PRINCIPLES

The following seven valuation principles are widely accepted as general foundations of business valuation.

i Principle 1: value is determined at a specific point in time

Value is determined at a specific point in time based on information that was known or knowable at that point in time. The value of a business interest is based on the market's perception at a specific point in time of the business' future prospects and in particular the future cash flow that the business is likely to generate.

The prospects for a business change from day to day as new information becomes available. Both external and internal factors continually impact the value of a business and, as such, value is determined at a specific point in time.

Consistent with this principle, hindsight information is generally excluded from consideration when determining value. In negotiating an open market transaction, the vendor and purchaser do not have the benefit of future information. The same principles are applied to valuation in a notional context, where value is to be based only on information that was known or knowable at the time of the valuation.

ii Principle 2: value is a function of the future benefits to accrue from ownership

Value is principally a function of the prospective future cash flows of a business. Potential acquirers evaluate a business based on expectations of the cash flow that will accrue to them following the acquisition. As the saying goes, 'cash is king'.

Value is therefore based on expected future performance as measured by the discretionary future cash flows to be received from the investment in the business. Value is a function of the prospective cash flows and the risk of achieving the future cash flows in the amount and timing anticipated. In assessing prospective cash flows, historical financial performance can be informative to the extent it is representative of future performance; however, a valuator must consider evolving industry and economic trends.

iii Principle 3: the market dictates the rate of return

Conceptually, the value of a business is equal to the present value of the business' anticipated future cash flows. The rate of return used to determine the present value of the future cash flows is derived from market rates of return. At any given time, investors must weigh an investment of capital in a business or asset against other potential investments available in the marketplace.

Market rates of return are based on general market forces, which include:

- a* general economic conditions including short- and long-term borrowing rates. Borrowing rates impact the acquisition and divestiture activities of investors and the rates of return required by purchasers on their invested capital;
- b* the market's perception of a certain industry and the risk profile of the industry. This includes the market's perception of the risks, opportunities, competitive landscape, regulatory environment and growth prospects of an industry;
- c* the types of purchasers in the market, their investment objectives and motivations; and
- d* company-specific risk factors unique to the business being valued.

The market-driven rate of return reflects the rate of return necessary to motivate investors to deploy capital in the business given the associated risk and opportunities of achieving the projected cash flows. At any point in time, a market-driven equilibrium exists whereby the rate of return offered by a particular investment vehicle reflects the market's perception of the investment risk of that vehicle. Investors seek to maximise their return while minimising their risk.

In determining business value, the prospective cash flows of a business and the rate of return applied to those cash flows are interdependent. The higher the risk of realising the cash flows, the higher the required rate of return.

iv Principle 4: value is influenced by liquidity

In general, the greater the liquidity of an investment, the greater the value of that investment. Liquidity is a measure of the ability to convert an investment into cash. A liquid investment

is one that can be quickly converted into cash. Greater liquidity reduces the risk of an investment by providing the potential purchaser with a greater ability to access their capital and exit their investment.

The liquidity of an investment in a private business is often restricted by certain provisions contained in shareholders' agreements or corporate articles. It is not uncommon for shareholders' agreements to limit the ability of shareholders to transfer their shares. In such circumstances the valuator may assess the impact of such provisions on value and, if appropriate, reduce the value by applying an appropriate 'liquidity' discount.

v Principle 5: value of a minority interest versus a controlling interest

The value of a minority interest is generally less than the value of a controlling interest considered on a *pro rata* basis.

A controlling shareholder is generally defined as a shareholder that through their ownership interest can elect the majority of the board of directors and in turn govern the business operations. The fair market value of a controlling interest is generally determined on a *pro rata* basis by applying the ownership interest percentage of the controlling shareholder to the 'en bloc' fair market value.

A minority shareholder does not have the same ability to influence the business decisions and operations of the business or dictate the amount or timing of dividends or the terms and conditions and timing of the eventual sale of the business. As such, the value of a minority interest may be less than the *pro rata* portion of fair market value.

A minority discount is often applied when arriving at a value conclusion for the minority interest to account for the minority interest's inability to influence and control the operations of the business. The quantum of the minority discount is fact and case specific and based on the valuator's consideration of the ownership structure, relationship between the owners, agreements between the owners, statutory provisions on business governance and shareholder rights, as well as other relevant information.

vi Principle 6: value is influenced by the underlying net tangible assets

Tangible assets consist of a business' physical assets and include working capital, inventory, property, plant and equipment. In general, all else held constant, a higher tangible asset base reduces the risk profile of a business and supports a higher business value.

A higher tangible asset base generally reduces the risk associated with the business because it:

- a* provides a natural barrier to entry. The large capital investment required to enter capital intensive industries often serves as a natural barrier to entry for potential new competitors and limits the risk of competition;
- b* increases a business' collateral and provides greater access to debt financing. Lenders are generally more comfortable extending credit to businesses with strong collateral. Increasing the relative proportion of debt in the company's overall capital structure can lower the company's overall cost of capital (since the cost of debt financing is generally less than the cost of equity financing); and
- c* reduces downside risk. If all else fails and the business is not successful, a potential acquirer has lower downside risk in an investment in a business with a high net tangible asset base as the assets of the business can be sold, thereby limiting the total loss of the failed enterprise.

vii Principle 7: commercial and non-commercial value are distinct

Successful companies have, to a greater degree than less successful companies, intangible qualities that result in the business earning comparatively larger cash flows and returns. The incremental value created by these intangible qualities is commonly referred to as goodwill.

Goodwill is an intangible asset that reflects a business' established brand, reputation, customer loyalty and other intangible factors that cannot be separately identified or quantified. Goodwill consists of both those assets that can be transferred to a potential purchaser and are commonly referred to as commercial goodwill, and those that cannot be transferred and are commonly referred to as personal or non-commercial goodwill.

The commercial value of a business is derived from the business' assets and operations and includes commercial goodwill. The non-commercial component of value is a function of the personal abilities or relationships of an individual and do not accrue to a potential acquirer. A potential acquirer will generally not pay for personal goodwill as it is non-transferable.

V FUNDAMENTALS OF BUSINESS VALUATION

Enterprise value versus equity value

Enterprise value and equity value are two value terms that are often misunderstood. The value of a business interest consists of two components: (1) the value of the business' equity; and (2) the value of the business' outstanding debts. Together these two components comprise the enterprise value of the business, which represents the value of the business in its entirety including its equity and debt components. Enterprise value is not affected by how a business is financed.

In contrast, the equity value of a business represents the value of a business's equity (i.e., the value of the shares) and is equal to the enterprise value less the value of the business' net debt. The equity value is affected by how a business is financed.

The enterprise value of a business comprises the value of interest-bearing debt and equivalents, plus the value of the business' net operating assets (cash, inventory, receivables less payable and fixed assets), plus the value of identifiable intangible assets (brand names, trademarks) and non-identifiable intangible assets (commercial goodwill). Equity value excludes the value of interest-bearing debt and equivalents and represents the shareholder's or owner's claim to the business' assets.

VI VALUATION APPROACHES AND METHODOLOGIES

i General value approaches

There are three generally accepted approaches to valuing an asset or business.

Income or cash-flow approach

The value of the asset or business is determined based on the expected future cash flows to be generated by the asset or business. The prospective future cash flows are discounted or capitalised at an appropriate rate of return reflective of the risks inherent in realising the cash flows.

Cost approach

The value of the asset is determined based on the historical cost of the asset or the cost to replace the asset. The cost approach is typically reserved for the valuation of specific assets rather than in the determination of the value of an active business as a whole.

Market approach

The value of the asset or business is determined based on the application of comparable market valuation metrics. The underlying premise is that the metrics associated with a comparable asset or business reflect the inherent risks of that asset or business and are applicable to the business subject to valuation.

ii Liquidation approach versus going concern approach

The first step in assessing the value of a business is to assess the viability of the business. The valuator must assess whether the business is expected to realise a reasonable rate of return on the value of the net assets employed in the venture. This analysis will inform the valuator's decisions of whether to employ a going-concern approach or a liquidation approach.

Going concern approach

The value of the business is determined based on the underlying assumption that the business will continue to operate and generate positive prospective future cash flows.

Liquidation approach

Represents the estimated net proceeds that would remain following the disposition of the business' underlying assets and settlement of its liabilities.

Selection of valuation approach

A business that is considered to be economically viable is generally valued on a going-concern basis implying that the business will continue to operate into the future. A going-concern valuation approach focuses on the future economic benefits (the prospective cash flows) that will accrue to the ownership group.

A business that generates recurring negative cash flows, or where the business is not expected to realise a reasonable rate of return on its invested capital, will typically be valued on a liquidation basis. A liquidation approach assumes that the business' assets will be sold, its debts repaid, and any proceeds will be distributed to the equity holders. The premise underlying a liquidation scenario is that the maximum value to the shareholders will be realised not by continuing to operate the business, but rather by converting the net assets of the business back to cash so that the shareholders can redeploy this capital into another (more promising) business venture. When value is to be determined pursuant to a liquidation approach, an asset-based valuation methodology is generally used. Liquidation analysis may be either on an orderly basis, meaning the business is assumed to have a reasonable timeline to wind down its operations and maximise value, or forced, where an expedited timeline is assumed.

iii Valuation methodologies

Asset-based valuation methodology

Pursuant to an asset-based valuation methodology, the value of a business interest is determined based on the value of the business' underlying assets and liabilities. Asset-based valuation methodologies are most commonly employed when valuing holding companies (companies whose primary function is to hold investments in other businesses) or when the valuator determines that an operating company is not viable (and a liquidation valuation approach is therefore employed as the primary valuation technique).

The most commonly employed asset-based valuation methodology is the adjusted net book value methodology. Pursuant to the adjusted net book value methodology, the valuator adjusts the reported book value of the subject business' assets and liabilities to reflect fair market value at the valuation date.

It is important to understand that the book values reported on a company's balance sheet often reflect historical cost amounts or may not reflect the true economic value of an asset or liability. For example, reported asset values on a balance sheet often reflect the initial purchase price of an asset that may or may not be indicative of fair market value at the valuation date.

In general, the adjusted net book value methodology involves adjusting the reported shareholders' equity as reported on a company's financial statements by adding or deducting the amount by which the value of the net assets exceeds or is less than the value reported for accounting purposes and adjusting for related tax differences.

The adjusted net book value methodology can be applied in both a going-concern and a liquidation value scenario. Under a liquidation approach, value is calculated as the difference between the net realisable value of the business' assets and the amounts needed to satisfy the business' liabilities. In these calculations, the net realisable value of a particular asset is the cash retained by the business from the sale of each asset after paying any sales commissions, moving costs, taxes and other costs incurred to dispose of the asset and effect the winding up of the business.

Cash flow and earnings-based valuation methodologies

Cash flow-based valuation methodologies are commonly employed when the underlying business interest is determined to be a viable operating enterprise. The two most common cash flow-based valuation methodologies are the capitalised cash flow (or earnings) methodology and the discounted cash flow methodology.

Cash flow or earnings-based valuation methodologies require:

- a* an informed assessment of the prospective future cash flows of the business being valued;
- b* an assessment of the risk of achieving the projected future cash flows both in quantum and on the anticipated timeline. The risk assessment informs the valuator's estimate of the appropriate risk adjusted rate of return (or valuation multiple) to apply when estimating the business' enterprise value;
- c* an analysis and assessment of the fair market value of the business' interest-bearing debt and equivalents at the valuation date. Interest bearing debts and equivalents are deducted from enterprise value to determine the equity value of the business; and
- d* an analysis of the business' net assets. The calculated enterprise value assumes that the business has adequate operating assets (i.e., working capital, fixed assets) to generate the projected cash flows. Where the business does not have adequate assets, an adjustment

is required to account for a shortfall. Similarly, when the business holds excess assets that are not required for the ongoing operations of the business, the fair market value of these redundant assets are added to arrive at the equity value of the business.

The capitalised cash flow/earnings methodology

The capitalised cash flow (or earnings) methodology involves dividing an estimate of a business' normalised maintainable after-tax discretionary cash flow by an appropriate capitalisation rate that reflects the risks and rewards of the business. The capitalised cash flow methodology is based on the assumption that a business' future cash flows will be relatively stable from year to year or increase at a stable rate of growth. As a result, this methodology is typically adopted for mature businesses with relatively stable earnings that can be reasonably estimated into perpetuity or when a reasonable forecast of cash flows is not available.

Pursuant to the capitalised cash flow methodology the valuator first estimates the company's annual maintainable discretionary cash flow. Discretionary cash flow is the quantum of cash flow earned by the business that can be distributed to the shareholders of the business each year without impairing the business' ongoing operations.

Estimating a reasonable maintainable cash flow level requires professional judgement and analysis of the business and its prospects, including the prevailing and prospective economic and industry conditions. Maintainable cash flow is often expressed as earnings before interest, taxes, depreciation and amortisation or EBITDA.

To estimate a company's maintainable cash flow a valuator typically considers:

- a* the historical operating results of the company. Historical operating results provide an objective benchmark upon which future operating levels may be estimated. However, it is important that the historical results are reviewed in the context of prevailing market conditions; and
- b* contemporaneously prepared forecasts, business plans and budgets. A well-formulated budget provides insight into management's expectations and may reveal business trends or factors that should be considered in assessing maintainable earnings. Business plans, budgets and forecasts are often prepared by management as part of their annual planning.

The analysis of a business' historical and prospective cash flows should also consider the need for any adjustments to normalise the business' performance. Normalisation adjustments are required to account for non-recurring, unusual and non-discretionary amounts and may include adjustments to:

- a* eliminate the impact of non-recurring or unusual historical revenue or expense amounts including, for example, start-up costs, one-time litigation costs, moving expenses and restructuring charges;
- b* reflect adjustments to related-party compensation (salaries and bonus) paid to owners and managers to the extent the reported compensation expense does not reflect a fair market value for the services rendered;
- c* adjust other non-arm's-length transactions to reflect a fair market rate. For example, it may be necessary to adjust rent payments if such payments are paid to a related party and are below market rates; and
- d* eliminate income or expenses related to redundant assets as it is assumed that these assets are not required for the ongoing operation of the business. The fair market value of redundant assets is separately added to value.

Based on the foregoing, the valuator estimates a range of maintainable cash flow. From this maintainable cash flow, the valuator deducts corporate income taxes, sustaining capital expenditure requirements⁴ and incremental working capital requirements to arrive at an estimate of the company's after-tax maintainable discretionary cash flow.

Components of discretionary cash flow
Earnings as reported on the financial statements
+/- Non-cash adjustments (depreciation, amortisation, etc.)
+/- Normalisation adjustments (non-recurring and related party)
Maintainable earnings
Less: Corporate income taxes
Less: Working capital requirements
Less: Capital expenditure requirements
After-tax discretionary cash flows

The second step of the capitalised cash flow methodology is to estimate the present value of the future cash flow by dividing the estimated maintainable cash flow by an appropriate risk adjusted capitalisation rate. The capitalisation rate reflects the valuator's assessment of the risk of the business realising the maintainable cash flow.

The selection of a capitalisation rate is subjective and is based on the professional judgement, experience and the knowledge of the valuation professional. The valuator may consider:

- a prevailing market rates of return, including the prevailing risk-free rate (often measured with reference to government bond rates) and equity risk premiums (measure with reference to public equity market returns);
- b industry risk factors and prevailing market rates of return for industry participants;
- c company specific risk factors, including an analysis of the principal strengths and weaknesses and the opportunities and threats facing the company at the valuation date. The valuator will consider the company's customer relationships, client concentration, stability and predictability of earnings etc.;
- d an appropriate capital structure of the subject company having consideration for the debt capacity of the subject company, its existing lending arrangements and the capital structure of comparable companies; and
- e the prevailing and prospective corporate income tax rate.

The capitalised cash flow of the subject company is calculated by dividing the estimated maintainable discretionary cash flow by the selected capitalisation rate. To the capitalised cash flow, the present value of the existing tax pools is added to arrive at enterprise value. To determine equity value the fair market value of redundant assets, if any, is added and interest-bearing debt and debt equivalents outstanding at the valuation date are deducted.

⁴ Sustaining capital expenditure requirements are the annual capital cost required to sustain the operations of the business. It represents the annual required investment in a company's capital assets.

The following table illustrates the capitalised cash flow methodology.

Capitalised cash flow illustration		
	Low	High
Selected maintainable EBITDA	US\$90,000	US\$100,000
Less: corporate income taxes	(23,850)	(26,500)
After-tax cash flows	US\$66,150	US\$73,500
Less: incremental working capital requirements	(5,000)	(5,000)
Less: sustaining capital expenditure (net of the tax shield)	(10,000)	(10,000)
Maintainable after-tax cash flows	US\$51,150	US\$58,500
Divide by: capitalisation rate	11.0%	12.0%
Capitalised cash flow	US\$465,000	US\$487,500
Add: present value of UCC tax shield	10,000	10,000
Enterprise value	US\$475,000	US\$497,500
Add: redundant assets	500	500
Less: interest bearing debts and equivalents	5,500	5,500
Equity value/fair market value	US\$470,000	US\$492,500

Discounted cash flow methodology

Whereas the capitalised cash flow approach is based on a single annual estimate of maintainable cash flows, the discounted cash flow (DCF) valuation methodology involves forecasting the year-by-year cash flows of the subject company for a specified number of years. The present value of each of these future amounts is then calculated based on the valuator's estimate of the appropriate risk-adjusted required rate of return (discussed previously).

In addition to the forecast period cash flows, most businesses will continue to earn cash flows after the forecast period. The value of these post-forecast period cash flows is referred to as the terminal value. The valuator estimates terminal value based on an estimate of the business' annual maintainable cash flow in the post-forecast period capitalised at an appropriate rate of return. The calculation of the residual value is in essence a capitalised cash flow approach bolted on to the DCF analysis.

The net present value of the cash flows during the forecast period and the terminal period are added to determine the enterprise value of the business. To determine the equity value, interest-bearing debts are deducted and redundant or deficient assets are added or subtracted.

A DCF methodology is typically appropriate where the business has relatively sophisticated business-planning protocols, where the business is expected to experience variable production over several years and for assets with limited economic lives (e.g., mines).

The following chart illustrates the DCF methodology.

Discounted cash flow illustration				
	Forecast period			Terminal period
	Year 1	Year 2	Year 3	
EBITDA	US\$5,000	US\$10,000	US\$20,000	US\$20,400
Less: corporate income taxes	(1,250)	(2,500)	(5,000)	(5,100)
Less: working capital requirements	(500)	(500)	(1,000)	(40)
Less: sustaining capital reinvestment	(1,000)	(1,000)	(1,000)	(1,000)
After-tax discretionary cash flow	US\$2,250	US\$6,000	US\$13,000	US\$14,260
Capitalisation rate				8.0%
Terminal value				\$178,250
Discount rate	10.0%	10.0%	10.0%	10.0%
Discount period (number of years)	0.5	1.5	2.5	2.5
Discount factor	0.953	0.867	0.788	0.788
Net present value of cash flows	US\$2,145	US\$5,201	US\$10,244	US\$150,308
Sum of the present value of the cash flows during the forecast period				US\$17,590
Present value of the terminal period cash flows				150,308
Enterprise value				US\$167,898
Less: interest bearing debt and equivalents				(10,000)
Add: redundant assets				5,000
Equity value/fair market value				US\$162,898

Market-based valuation methodologies

The market-based valuation approach relies on public equity market data and precedent transaction data of companies determined to be somewhat comparable to the subject company being valued. This valuation methodology involves analysing the valuation multiples, financial ratios and operating results of these comparable companies and transactions and applying those multiples to the subject company. The underlying premise of the market-based approach is that companies in similar industries face similar risks and as a result should have similar return profiles.

The two principal market-based valuation approaches are (1) the comparable public company approach, and (2) the precedent transaction approach.

Comparable company approach

A comparable company approach involves researching and calculating the valuation metrics and financial ratios of publicly traded companies that are deemed to be somewhat comparable to the subject company. In these cases, the valuator may consider 'value benchmarks' in his or her analysis.

Examples of valuation benchmarks include:

- a enterprise value to EBITDA multiple – calculated as enterprise value divided by EBITDA;
- b enterprise value to revenue multiple – calculated as enterprise value divided by revenue;
- c price-to-book-value ratio – calculated as the public market capitalisation of the company divided by the reported net book value of the company; and

- d* price-to-earnings ratio – calculated as the public market share price divided by the earnings per share.

There are many other valuation ratios that are commonly calculated. Some ratios are more relevant to one industry than another. Given the inherent difficulties in identifying reasonably comparable companies, the comparable company approach is most often used as a secondary valuation approach, to assess the reasonableness of the notional valuation conclusion based on a cash flow or asset-based methodology.

Precedent transactions approach

Precedent transaction analysis involves researching and reviewing actual transactions involving companies that are comparable to the subject company. Utilising publicly disclosed information about actual transactions including the selling price, historical performance and terms and conditions of sale, it is possible to determine comparable valuation metrics that can then be applied to the subject company to determine a value conclusion. Similar multiples as those illustrated above can be determined for these precedent transactions.

Rules of thumb

In certain industries, market rules of thumb may exist that can be used to determine business value. Rules of thumb are generally applied as a secondary test of the reasonableness of a value conclusion arrived at through a cash flow or other valuation methodology. Rules of thumb have their foundations in market transactions involving companies in a specific industry and are based on industry-specific activity ratios or formulas that have been derived over time. When using a rule-of-thumb approach, it is important that the valuator considers what exactly the rule of thumb is calculating and whether the rule of thumb is applicable to the business interest being valued.

VII CONCLUSION

Business valuation is an inherently subjective exercise. In preparing a business valuation, valuation professionals apply their professional judgement, experience and knowledge of business valuation fundamentals to the specific facts to arrive at an informed and reasoned value conclusion. Whether for the purpose of calculating damages from a capital loss or otherwise, it is generally advised that a business valuation professional be consulted when a business valuation is required.

Part II

JURISDICTIONS

AUSTRALIA

*Simon Morris, David Winterton and Amir Chowdhury*¹

I OVERVIEW

In Australia, monetary relief is available under common law, equity and statute. Determining whether a plaintiff is entitled to a damages award and the quantum of that award will require consideration of those three sources of law, the type of claim being made and the remedial purpose of the award.

i Common law

At common law, damages generally serve a compensatory purpose for the defendant's tort or breach of contract. The monetary remedy normally aims to place the plaintiff in the position he, she or it would have been in had the breach of duty not been committed.

ii Equity

Both equitable compensation and an account of profits are generally available for breaches of equitable obligations. Equitable compensation can be distinguished from damages by the characteristics unique to it, including its discretionary nature. An account of profits focuses on the gains made by the defendant via breach of the relevant equitable obligation rather than on the plaintiff's loss.

iii Statute

Statute will often also provide a monetary remedy. The extent to which common law or equitable principles apply to such a claim is a question of statutory construction. The questions of construction that the court will need to consider will be whether and to what extent the statutory provisions modify the operation of general law principles. As such, the measure of relief will be dependent on the particular statutory provision.

iv Non-compensatory damages

Punitive, gain-based and liquidated damages also may be available in exceptional circumstances where compensatory damages are deemed to be an inappropriate response to the breach.

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v Punitive and exemplary damages

Punitive damages are occasionally awarded for certain wrongs recognised by common law to punish the wrongdoer and deter the commission of future wrongs, but the traditional view is that they are not available for breaches of equitable obligations.²

vi Restitutionary damages

The availability of a gain-based award in response to a common law wrong has occasionally been recognised, most often in cases where the defendant tortiously interfered with the plaintiff's right to goods³ or land.⁴ The term 'restitutionary damages' is sometimes used as a label to describe all such awards for common law wrongdoing, but it has also been suggested that it is necessary to distinguish between two measures of gain in this context: one based on the immediate transfer of value to the defendant that is entailed by the wrong and one based on the consequential profits that accrue to the defendant as a result of the wrong, which is sometimes labelled 'disgorgement'.⁵ While both measures of gain have also exceptionally been awarded for breach of contract in England, Australian courts have been reluctant to allow for gain-based recovery for contractual breach.⁶

vii Liquidated damages

At common law, liquidated damages are available where parties contract for a fixed amount of damages to be payable for a breach of contract in circumstances where the predetermined amount is a genuine pre-estimate of the loss likely to flow from the breach rather than a sum intended to punish or deter the breach. Equity may also deem a sum payable on the happening of an event other than breach ('the primary stipulation') 'penal' and hence irrecoverable where it is 'out of all proportion' to the interests protected by the primary stipulation,⁷ or where it 'is properly characterised as having no purpose other than to punish'.⁸

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

The aim of awarding damages, at least in commercial cases, is generally to put the plaintiff in the financial position he, she or it would have been in had the relevant breach of duty not occurred.⁹ But in upholding this principle, various subsidiary matters arise, including how

2 See *Harris v. Digital Pulse Pty Ltd* (2003) 56 NSWLR 298 (Heydon JA).

3 See *Bunnings Group Ltd v. CHEP Australia Ltd* [2011] NSWCA 342; (2011) 82 NSWLR 420 at [172]-[175], [177]-[178], considering damages assessment for conversion or detinue.

4 For trespass to land, see *Houghton v. Immer (No. 155) Pty Ltd* (1997) 44 NSWLR 46 and *Inverugie Investments v. Hackett* [1995] 1 WLR 713 (PC).

5 See J Edelman, *Gain-Based Damages: Contract, Tort, Equity and Intellectual Property* (Hart 2002).

6 See *Hospitality Group Pty Ltd v. Australian Rugby Union Ltd* 110 FCR 157. Compare *Attorney General v. Blake* [2001] 1 AC 268.

7 See *Paciocco v. Australia and New Zealand Banking Group Ltd* (2016) 258 CLR 525; [2016] HCA 28, [57] (French CJ and Kiefel J).

8 *ibid*, [165] (Gageler J).

9 *Livingstone v. Rawyards Coal Co* (1880) 5 App Cas 25, 39 (Lord Blackburn).

the plaintiff's counterfactual financial position is to be quantified and which consequences resulting from the breach are included in this assessment. A number of these subsidiary matters are now addressed.

ii Evidence

A plaintiff claiming damages is expected to adduce evidence that is available and typically adduced in that type of claim. Where a plaintiff does not adduce such evidence, he or she cannot complain of the non-award of damages or of a lesser quantum of damages than would have been obtained if the evidence had been adduced.¹⁰

iii Date of assessment

Typically damages arising from a breach of contract are assessed at the date of the breach, but courts will depart from this general rule 'whenever it is necessary to do so in the interests of justice'.¹¹ Damages arising from a tort are also typically assessed at the date on which the cause of action arose. However, in personal injury cases and death cases, damages are normally assessed at the date of judgment.¹²

Mitigation

It is important for a plaintiff to identify the applicable date of assessment for its cause of action as it will affect the date from which the court expects a plaintiff to act reasonably and attempt to minimise loss caused by the defendant's wrongdoing.¹³ If the plaintiff failed to act reasonably, he or she will not be awarded damages for losses that could reasonably have been avoided.¹⁴ Plaintiffs who take reasonable steps to mitigate loss are entitled to be compensated for the costs of taking such reasonable steps, even where the costs of taking such action overall increases the loss suffered.¹⁵

iv Financial projections

Future loss

Damages must compensate the plaintiff on a once-and-for-all basis. As such, the lump sum award must encompass not only the loss already suffered by the plaintiff but also any causally attributable losses that the plaintiff is likely to suffer in future. A plaintiff will be entitled to an award of damages to compensate future loss if he or she can establish, on the balance of probabilities, that the defendant's wrongdoing caused loss of a non-negligible opportunity that the plaintiff would have taken advantage of.

v Assumptions

In quantifying the plaintiff's loss, a court may be entitled to make certain assumptions about the value of what has been lost or about what would have happened had the breach not occurred. For example, the value of goods tortiously damaged or not delivered in breach of

10 *Luna Park (NSW) Ltd v. Tramways Advertising Pty Ltd* (1938) 61 CLR 286.

11 *Johnson v. Perez* (1988) 166 CLR 351, 356.

12 *O'Brien v. McKean* (1968) 118 CLR 540.

13 *Simply Irresistible Pty Ltd v. Couper* [2010] VSC 601.

14 *Hasell v. Bagot, Shakes & Lewis Ltd* (1911) 13 CLR 374, 388.

15 *Fox v. Wood* (1981) 148.

contract is generally measured by reference to the market price, at least where an available market exists, and it may be that, when a plaintiff claims damages following an acceptance of the defendant's contractual repudiation, it is assumed that the plaintiff would have been able to perform its own remaining obligations under the contract.¹⁶ It is a matter of debate as to whether these various assumptions are necessarily rebuttable or are sometimes irrebuttable.

vi Discount rates

Above we described circumstances where a plaintiff can claim for loss of opportunity and future losses. If the plaintiff is awarded damages to compensate for loss that has yet to occur, the plaintiff is essentially receiving an advance payment of that loss. An adjustment must be made to account for the accelerated receipt in the form of discounting the damages to present value.¹⁷

In commercial cases, market rates of interest will be considered an appropriate discount rate,¹⁸ but in personal injury and death cases, state jurisdictions have their own statutory provisions prescribing fixed a discount rate. In the Northern Territory, New South Wales, Queensland, South Australia and Victoria the discount rate is 5 per cent.¹⁹ In Western Australia the discount rate is 6 per cent.²⁰

vii Currency conversion

Damages awarded in foreign currency will generally be converted into Australian dollars using the spot foreign exchange rate at the date of judgment.²¹

viii Interest on damages

Courts in most Australian jurisdictions²² have a statutory discretion to award interest on damages.²³ Common to those jurisdictions are three principles that courts must have regard to when exercising their power to award interest on damages.

First, the power is discretionary, and depending on legislation, the court must consider whether or not to award interest, for what period the interest calculation is to run, the rate of interest and on what portion of damages that interest will be applied. Second, the object of the power to award interest is to compensate plaintiffs for being kept out of damages and

16 See the discussions in *YP Barley Producers Ltd. v. Robertson (EC) Pty Ltd* [1927] VLR 194 and, more recently, *Flame SA v. Glory Wealth Shipping Pte Ltd (The Glory Wealth)* [2013] EWHC 3153 (Comm).

17 *Sellars v. Adelaide Petroleum NL* (1994) CLR 332.

18 *Pennant Hills Restaurants Pty Ltd v. Barrell Insurances Pty Ltd*; sub nom *Barrell Insurances Pty Ltd v. Pennant Hills Restaurants Pty Ltd* (1981) 145 CLR 625.

19 Personal Injuries (Liabilities and Damages) Act 2003 (NT) Section 22; Civil Liability Act 2002 (NSW) Section 14; Civil Proceedings Act 2011 (Qld) Section 61; Civil Liability Act 1936 (SA) Sections 3 and 5; Civil Liability Act 2001 (Tas) Section 28A; Wrongs Act 1958 (Vic) Section 28I.

20 Law Reform (Miscellaneous Provisions) Act 1941 (WA) Section 5.

21 *Brown Boveri (Aust) Pty Ltd v. Baltic Shipping Co* (1989) 15 NSWLR 448, 464.

22 But not in Tasmania.

23 Judiciary Act 1903 (Cth) Section 77MA(2)(a); Federal Court of Australia Act 1976 (Cth) Section 51A(2)(a); Federal Circuit Court of Australia Act 1999 (Cth) Section 76(4)(a); Court Procedures Rules 2006 (ACT) r1616(6)(a); Supreme Court Act 1979 (NT) Section 74(2)(a); Civil Procedure Act 2005 (NSW) Section 100; Civil Proceedings Act 2011 (Qld) Section 58; Supreme Court Act 1936 (SA) Section 30C(4)(a); District Court Act 1991 (SA) s39(4)(a); Magistrates Court Act 1991 (SA) Section 34(4)(a); Supreme Court Act 1986 (Vic) Section 60(2)(a); Supreme Court Act 1935 (WA) Section 32(2)(a).

so the *prima facie* time for when interest starts to accrue is the point in time when the breach is said to have occurred.²⁴ Third, the statutory provisions regarding interest do not apply to cases of dishonoured bills of exchange.²⁵

ix Costs

Costs generally follow the event, meaning that the successful party is entitled to recover costs from the other side unless there is a good reason to justify a contrary order.²⁶ Reasons that might deprive a successful party from recovering its costs include where the damages awarded are ‘nominal’,²⁷ where the successful party misbehaved in relation to either the subject of the conduct of the proceedings or where the successful party rejected a settlement offer or offer of compromise, and failed to obtain an order or judgment on the claim no more favourable to such offer.²⁸

x Tax

Awards of damages may be subject to taxation if categorised as income, indemnity or capital gain. Losses that would have been taxable, but for the wrong, and which then form the basis for an award of damages, will not necessarily still be considered taxable. An example of such losses are those forming the basis for an award of damages in certain personal injury cases.²⁹

III EXPERT EVIDENCE

i Introduction

A plaintiff seeking an award of damages must establish and assess losses suffered with as much certainty as the circumstances permit. Expert evidence can assist in persuading the court whether on balance the threshold of certainty has been met. Expert evidence adduced to assist the court in calculating damages are subject to the same rules of expert evidence in general.

ii The role of expert evidence in the calculation of damages

Expert evidence is particularly useful where scientific, technical or other specialised knowledge might assist the court in understanding evidence or facts at issue.

The common law position is that expert evidence cannot usurp the role of a judge in his or her function in calculating damages. If experts were allowed to answer the ‘ultimate issue’, and the answer is accepted by the court, then ‘the chances of success on an appeal on fact are

24 *Grincelis v. House* (2000) 201 CLR 321.

25 Judiciary Act 1903 (Cth) Section 77MA(2)(c); Federal Court of Australia Act 1976 (Cth) Section 51A(2)(c); Federal Circuit Court of Australia Act 1999 (Cth) Section 76(4)(c); Court Procedures Rules 2006 (ACT) r1616(6)(c); Supreme Court Act 1979 (NT) Section 74(2)(c); Civil Procedure Act 2005 (NSW) Section 100(3)(d); Civil Proceedings Act 2011 (Qld) Section 58(4)(b); Supreme Court Act 1935 (WA) Section 32(2)(c).

26 *Milne v. A-G (Tas)* (1956) 95 CLR 460, 477.

27 *Alltrans Express Ltd v. CVA Holdings Ltd* [1984] 1 All ER 685;

28 *Singleton v. Macquarie Broadcasting Holdings Ltd* (1991) 24 NSWLR 2013, 108, Uniform Civil Procedure Rules 2005 (NSW) Rules 42.15-42.15A.

29 *Atlas Tiles v. Briers* (1978) 144 CLR 202, 223.

slight indeed, since there is direct and acceptable evidence on the very point at issue'.³⁰ This 'ultimate issue' rule does not prevent questions being put to the expert witness that causes him or her to consider a hypothetical scenario where he or she is asked to assume the facts stated in evidence to be true.³¹

The common law's 'ultimate issue' rule has been abolished by statute.³² Although expert evidence cannot be deemed inadmissible solely because it goes to an 'ultimate issue', the rule still has utility as a caution for judges to 'exercise particular scrutiny when experts move close to the ultimate issue, lest they arrogate expertise outside their field or express views unsupported by disclosed and contestable assumptions'.³³

iii The court's role in excluding and managing expert evidence

Courts are able to consider and manage expert evidence that goes to proving the quantum of damages in accordance with the same principles in the assessment expert evidence generally. The Evidence Act³⁴ contains provisions addressing the admissibility of expert opinion. Although not all expert evidence is opinion, the rules relating to the admissibility of non-opinion expert evidence are generally analogous to that of expert opinion.

Generally evidence of an opinion is not admissible to prove the existence of a fact about the existence of which the opinion was expressed.³⁵ This exclusionary opinion rule does not apply if the person expressing the opinion has specialised knowledge based on the person's training, study or experience, and that opinion is wholly or substantially based on that knowledge.³⁶

Heydon JA's judgment in *Makita*³⁷ provides a summary of the principles relating to the admissibility of expert opinion:

In short, if evidence tendered as expert opinion evidence is to be admissible, it must be agreed or demonstrated that there is a field of 'specialised knowledge'; there must be an identified aspect of that field in which the witness demonstrates that by reason of specified training, study or experience, the witness has become an expert; the opinion proffered must be 'wholly or substantially based on the witness's expert knowledge'; so far as the opinion is based on facts 'observed' by the expert, they must be identified and admissibly proved by the expert; and so far as the opinion is based on 'assumed' or 'accepted' facts, they must be identified and proved in some other way; it must be established that the facts on which the opinion is based form a proper foundation for it; and the opinion of an expert requires demonstration or examination of the scientific or other intellectual basis of the conclusions reached: that is, the expert's evidence must explain how the field of 'specialised knowledge' in which the witness is expert by reason of 'training, study or experience', and on which the opinion is 'wholly or substantially based', applies to the facts assumed or observed so as to produce the opinion propounded.

30 *Joseph Crosfield and Sons Ltd v. Techno-Chemical Laboratories Ltd* (1913) 29 TLR 378, 379.

31 *R v. Smith* (1915) 11 Cr App R 229, 238.

32 Evidence Act 1995 (Cth), Section 80; each jurisdiction in Australia has its own Evidence Act, but they have been made uniform throughout almost all Australian jurisdictions.

33 *R v. GK* (2001) 53 NSWLR 317 (per Mason P).

34 Evidence Act 1995 (Cth).

35 Evidence Act 1995 (Cth) Section 76.

36 Evidence Act 1995 (Cth) Section 79.

37 *Makita (Australia) Pty Ltd v. Sprowles* (2001) 52 NSWLR 705.

If all these matters are not made explicit, it is not possible to be sure whether the opinion is based wholly or substantially on the expert's specialised knowledge. If the court cannot be sure of that, the evidence is strictly speaking not admissible, and, so far as it is admissible, of diminished weight.

Where an expert's opinion is admissible, courts are still unlikely to be persuaded by the evidence or to accept the expert's conclusions in circumstances where the expert relied upon flawed assumptions. In *Norris v. Blake*,³⁸ the New South Wales Court of Appeal considered the differing opinions expressed by a number of experts that related to the respondent's likely life expectancy in a personal injury claim. The economic loss ultimately awarded was dependent on the respondent's life expectancy. The Court held that a relevant factor was the assumption held by many of the experts that the respondent would be in a persistent vegetative state. The Court went on to conclude that the primary judge was entitled to discount those opinions because of his Honour's finding that the respondent was not in fact in a persistent vegetative state.

iv Independence of experts

In most jurisdictions within Australia an expert can be retained by either one or multiple parties to the proceedings, but the expert must remember that his or her paramount duty is to the court and not the parties retaining them.³⁹ Experts are duty bound to assist the court impartially and so must maintain a level of independence.

v Challenging experts' credentials

A party can challenge an expert's credentials by asserting that the expert does not possess 'special knowledge, skill, experience or training about a matter'.

If the expert is found to not possess the relevant special knowledge, skill, experience or training about a matter, his or her evidence will be inadmissible.

In establishing whether or not the expert possesses the relevant special knowledge, skill, expertise or training, first the relevant field of expertise must be identified and then the judge must consider the skill of the witness purporting to be an expert.

Each opinion or piece of evidence adduced must then wholly or substantially fall within the identified field of the witnesses' expertise. A chartered accountant, although able to express opinions about accounting standards, cannot necessarily give evidence relating to the conduct of a company director.⁴⁰ Another example where opinion is not wholly substantially based on the witness' specialised knowledge is where a chartered accountant is retained to write a report in which he or she restates the books of a publicly traded company, where that company is alleged to have misrepresented its financial position. Assuming that the accountant has no other expertise, he or she cannot then also be retained to calculate the true market value of the company's shares had the company not misrepresented its financial position (i.e., the accountant cannot calculate the loss suffered by an investor who bought the company's shares). In that case, the latter opinion, although relating to and following on from the calculations based on accounting expertise, falls substantially outside the accountant's field of expertise.

38 (1997) 41 NSWLR 49, 79.

39 Expert witness code of conduct Sch 7 UCPR; Federal Court of Australia Expert Evidence Practice Note (GPN-EXPT), Annexure A.

40 *Australian Cement Holdings Pty Ltd v. Adelaide Brighton Ltd* [2001] NSCW 645, [6].

vi Novel science and methods

Experts engaged to quantify damages in securities actions use a method of quantitative linear regression involving event studies. Event studies aim to quantify effects on share price caused by information (or rather misinformation) released to the market. This method of quantification arose out of US securities fraud litigation. Event studies assume a semi-strong efficient capital market hypothesis and require experts to select a relevant market or industry share index and obtain data for the movement in that index over a relevant period and compare it to the share price of the subject company to establish statistically significant linear trend by way of regression analysis.⁴¹ Then by comparing the actual share price immediately after the disclosure of information and a predicted price using the aforementioned trend, an expert concludes that the difference in those prices is the dollar value attributable to the disclosure of the information.

IV RECENT CASE LAW

i Re HIH Insurance Ltd (in liq) [2016] NSWSC 482 (HIH Insurance [2016]) and Re HIH Insurance Ltd (in liq) [2017] NSWSC 380 (HIH Insurance [2017])

HIH Insurance [2016] and *HIH Insurance* [2017] related to multiple claims by investors who acquired shares in HIH Insurance Limited (HIH) at an artificially inflated market price. HIH was a public company listed on the ASX. It was placed into liquidation in 2001 and admitted that its FY1999 financial statements, FY2000 interim financial statements and FY2000 final statements contained representations that were misleading and deceptive.⁴² The statutory causes of action required investors to show that they had suffered loss ‘by’ the contravening conduct, in this case the misleading and deceptive financial statements.⁴³

Justice Brereton interpreted the word ‘by’ to express ‘the notion of causation without defining or elucidating it’.⁴⁴ Justice Brereton followed Mason CJ’s leading judgment in *March v Stramare*,⁴⁵ which stated that for a sufficient causal link to be established, it must be shown that the contravening conduct ‘caused or materially contributed to’ the loss.

Thus, Brereton J found that it was not necessary to prove each investor’s individual reliance on the misleading or deceptive financial statement and that a causal link could instead be established by showing that HIH made misleading or deceptive representations in relation to its financial statements, the market was deceived into a misapprehension that HIH was trading more profitably than it really was and had greater net assets than it really had, HIH shares traded at an inflated market price and investors paid that inflated market price to acquire shares, thereby suffering loss.⁴⁶ This causal link is referred to as indirect market-based causation.

The principle recognised by Brereton J is similar but not identical to the well-established ‘fraud-on-the market’ doctrine recognised by the United States Supreme Court in *Basic*

41 Justice Beach, ‘Structural and Forensic Developments in Securities Litigation’, International Commercial Law Conference, Inner Temple, Inns of Court, London, 29 June 2016.

42 *HIH Insurance* [2016] NSWSC 482, [3].

43 Trade Practices Act 1974 (Cth) Section 82(1); Corporations Act 1989 (Cth) Section 1005.

44 *HIH Insurance* [2016] NSWSC 482.

45 (1991) 171 CLR 506, 514.

46 *HIH Insurance* [2016] NSWSC 482, [75].

v. Levinson.⁴⁷ The key difference between the two doctrines is that, under the approach recognised in *HIH Insurance* [2016], there is no need to establish reliance, whereas the American doctrine provides plaintiffs with a presumption of reliance on the integrity of the market price of securities effected by the misrepresentation, which it is open to the defendant to rebut with sufficient evidence.

Following on from the *HIH Insurance* [2016] decision, in *HIH Insurance* [2017] Brereton J provided further guidance when calculating the quantum of loss in circumstances where a shareholder purchased shares while market price was inflated by misrepresentations, but then subsequently sold some of those shares within the inflated period. The approaches suggested for his Honour's consideration included a 'last-in-first-out' (LIFO) approach, a 'first-in-first-out' (FIFO) approach and a proportionate approach. A proportionate approach requires treating the shares sold during the inflationary period as being proportionately drawn from the shares owned prior to the inflationary period and the shares acquired during the inflationary period. Brereton J held the LIFO method to be the favoured approach because it requires the shareholder to account for any inflationary benefit received on a share sale.

ii **Stone v. Chappel** [2017] SASCFC 72

In *Bellgrove v. Eldridge*, the High Court of Australia famously held that following the provision of defective building work, the innocent party is entitled to recover the cost of rectification provided such work is necessary to produce conformity with the contract and a reasonable course of action to adopt in the relevant circumstances.⁴⁸ This principle was reaffirmed by the High Court more recently in *Tabcorp Holdings Ltd v. Bowen Investments Pty Ltd*,⁴⁹ but a persistent question remains regarding precisely what determines whether rectification work is 'reasonable', it having been observed that 'the Court's reasons in *Tabcorp* provide little guidance in relation to the application of... [this] qualification' and that as yet 'there has been no express identification in the Australian case law of any principle or policy underpinning the notion of unreasonableness'.⁵⁰

Following *Tabcorp*, it might reasonably have been thought that the recovery of such awards is easier in Australia than in England given the House of Lords' decision in *Ruxley Electronics and Construction Ltd v. Forsyth* to deny a homeowner's claim for the cost of reconstructing a swimming pool not built to the requisite depth on the ground that the expenditure necessary to rectify the defect was 'out of all proportion' to the benefit to be obtained from the work.⁵¹ However, the High Court in *Tabcorp* did stress that the facts in *Ruxley* were 'exceptional'⁵² and the South Australian Supreme Court's recent decision in *Stone v. Chappel* arguably supports the view that the Australian and English positions are not all that far apart.⁵³

In *Stone*, the plaintiff homeowners engaged a builder to construct an apartment according to a previously prepared plan, which required that the ceilings would be 2.7m high.

47 485 U.S. 224 (1988). The continued correctness of the doctrine was also approved in *Halliburton Co v. Erica P John Fund Inc.* 134 S Ct 2398 (2014).

48 (1954) 90 CLR 613, 617.

49 [2009] HCA 8; (2009) 236 CLR 272.

50 *Stone v. Chappel* [2017] SASCFC 72, [250]-[254] (Doyle J).

51 [1996] AC 344.

52 *Tabcorp Holdings Ltd v. Bowen Investments Pty Ltd* [2009] HCA 8; (2009) 236 CLR 272, [18].

53 [2017] SASCFC 72.

However, the ceilings were built on average approximately 40mm lower than the specified height and the apartment owners sought to recover damages assessed by reference to the cost of rectification.

After a first instance decision in favour of the builder, the homeowners' appeal was unanimously denied, though there was a noteworthy split in the Court's reasoning. For Doyle and Hinton JJ, the 'reasonableness' test was primarily about determining whether the contractual objective (also referred to as the homeowners' 'performance interest') had been sufficiently delivered. According to their Honours, it had been here because the unit was structurally sound and any additional 'aesthetic interest' in precise performance was also 'substantially achieved'.⁵⁴

Kourakis CJ, by contrast, identified various distinct considerations relevant to determining whether rectification costs are 'reasonable' in the relevant sense, including 'the adverse effect of the departure on the functional utility, amenity and aesthetic appearance of the building... the reasons, objectively ascertained and commonly known, for which the innocent party made the stipulation which was breached... the absolute cost of the rectification work and the disproportion between that cost and the value of the building and contract price... the diminution in commercial value of the building... the nature of the wrongdoer's fault for the defect; and the public interest in reducing economic waste'. Applying these considerations to the present case, his Honour concluded that despite there being a strong *prima facie* case for the award of rectification costs, ultimately such an award should not be made because rectification would cause a significant fire hazard and likely promote 'unconstructive litigation' from other tenants in the block so that, despite the Stones' (probable) honestly held intention to rectify, it was unlikely that rectification would actually occur.⁵⁵

54 *ibid* [286] (Doyle J) and [418]-[454] (Hinton J). Compare *Ruxley*, where the pool was built somewhere between 9 and 18 inches too shallow.

55 *ibid* [52]-[75].

BRAZIL

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I OVERVIEW

The Brazilian legal system, mainly based on codes and legislation, provides for two main categories of civil liability: (1) fault-based liability, based on the culpability theory, in which there must be evidence of the damages suffered, of the occurrence of a faulty act or omission (negligence, imprudence or malpractice) or wilful misconduct, and of the link of causation between the harmful conduct and the damage; and (2) strict liability, based on the risk theory and applied irrespective of the analysis of offender's fault or intention, in which there must be evidence of the act or omission (i.e., evidence of its occurrence, and not of the fault or intention motivating it), the damage allegedly suffered by the party and the link of causation between the conduct and the damage. While fault-based liability is the general rule, pursuant to the Brazilian Civil Code, strict liability applies to cases specified in the law (e.g., consumer rights under Law No. 8,078/1990, environmental matters under Law No. 6,938/81) or when the offender's activity, by its nature, implies inherent risks to third parties (e.g., a carrier of hazardous or flammable substances).

The injured party is entitled to a broad scope of claims for damages, divided into two categories: moral damages, related to anguish, pain and suffering, and damage to property, which comprehends not only the compensatory or actual damages (e.g., an immediate, concrete, proven injury or loss, such as the damage arising out of a wilful misconduct that caused a devaluation of trademark) and loss of profit (i.e., the foreseeable earnings, proven with reasonable certainty, that the injured party would have received in the ordinary course of events if the harmful conduct had not occurred).

In claims for moral damages, the court will assess the indemnification to be granted to the injured party based on the circumstances of the case and on the indemnification standards adopted by the case law in similar cases. In general, the indemnification must consider the financial capability of the parties and must be reasonable and proportional in relation to the repercussion of the injury in order to avoid the undue enrichment of the injured party. The indemnification for moral damages is generally assessed in court without the need for expert examination.

In claims for damages to property (compensatory or actual damages and loss of profit), the injured party has the burden to prove not only the existence of the conduct, but also the tangibility of the loss and its concrete extension. An expert examination is generally conducted during the litigation in order to evidence the damage and its figures – although

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confirming the occurrence of a harmful act or omission, there will be no indemnification if the expert examination confirms that such act or omission has caused no concrete damage with financial consequences to the injured party.

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

The quantification of the financial loss has proven to be a considerably burdensome procedural phase for the injured party when it comes to claims for compensatory damages and loss of profit, especially in complex cases. In these cases, a comprehensive, accurate expert examination is crucial for the injured party, as it will only be entitled to receive an indemnification if it is able to evidence not only the occurrence of a harmful conduct, but also the actual, concrete damage with financial consequences arising out of such conduct. Should the injured party be able to evidence only the former but not the latter, there will be no indemnification to be paid by the offender to the injured party as compensatory damages or loss of profit.

ii Evidence

Damage to property (for which a claimant may be entitled to compensatory damages and loss of profit) is generally evidenced by means of expert examinations conducted in the field of knowledge of the matter under scrutiny in each lawsuit. For instance, an engineering examination is needed in cases discussing construction defects on buildings; accountant and economic examination is needed in cases discussing financial loss and loss of profit; medical examination will take place in cases discussing medical malpractice; a chemical composition examination will be demanded in cases discussing defects in the chemical composition of the product; and trademark examination is needed in cases discussing counterfeit.

As addressed below in more detail, the expert examination will be conducted by an expert appointed by the court directly, and the parties will be granted the possibility of appointing their experts to assist the court expert in the production of the technical evidence.

The expert examination will assess the exact amount of the damage suffered by the injured party, comprehending both the damage arising immediately and directly out of the harmful conduct (actual or compensatory damage) and the earnings that the injured party failed to receive as a result of such conduct (loss of profit). There is no limitation in value for the amount of indemnification in Brazil, as it must correspond to the exact amount of the damage suffered by the injured party, compensating it as if the harmful act had never occurred.

Note that there is no law in Brazil authorising punitive damages in addition to compensatory damages or loss of profit, as the amount to be indemnified must correspond to the actual losses suffered by the party. Nevertheless, doctrine has developed a threefold function for the condemnation to pay moral damages, which should concomitantly (1) compensate the victim for the wrongful act that injured its morals and psyche; (2) punish the offender; and (3) prevent the wrongful act from happening again. To some extent, although it is still far from the US standards on punitive damages, this interpretation by the Brazilian doctrine ends up functioning as a sort of 'punitive damages' encompassed by the moral damage category.

iii Date of assessment

The compensatory damages and loss of profit will be assessed considering the date in which the harmful conduct has occurred. The expert appointed by the court will be granted access to all relevant information and documents of the case in order to prepare an expert report, which will take into account the date of the harmful act, the amount of the indemnification sufficient to fully compensate and hold the injured party harmless, and the interest and inflation that will accrue on the amount of indemnification.

Note that the injured party may take several years to file a claim against the offender in view of the applicable statute of limitation period (e.g., three years for torts), resulting in a scenario where the assessment of the damage will occur much later in time in relation to the date on which the harmful conduct actually took place. In such cases, it is important for the injured party to preserve the evidence it has at its disposal in order to be used in the future to substantiate a claim for damages. In order to protect the injured party's interests in the meantime, it may file a precautionary measure against the offender to produce pieces of evidence in advance in order to prevent it from deteriorating.

iv Financial projections

In Brazil, the damage to property that the injured party is entitled to claim compensation for includes (1) the immediate, concrete, actual loss caused by the harmful act or omission (actual or compensatory damages), and (2) loss of profit or revenue, defined as the earnings that the injured party would reasonably and probably have received if the harmful act or omission had not occurred – in this case, the injured party must objectively evidence the high probability of receiving the earnings as a result of the ordinary course of events, as it would be expected without the harmful conduct committed by the offender.

Depending on the underlying matter and on the commercial activities of the parties, the indemnification for loss of profit (e.g., loss of operating revenue) can reach much more substantial figures than those assessed to compensate the actual damage immediately arising from the same harmful conduct.

Under Brazilian law, only direct damage – those suffered by the injured party and that have a direct, immediate and close chain of causation with the harmful conduct – are subject to indemnification. Indirect damage is not indemnifiable, as only the party directly affected would have standing to sue. For instance, court precedents usually hold that the mere devaluation of shares or decrease in dividends arising out of the fraudulent conduct of senior managers causes only indirect damage to shareholders, as the directly harmed party would be the company itself – therefore, in this case, the company, and not the shareholders acting by themselves, would be the entity with standing to claim such loss.

v Assumptions

The assessment of compensatory damages and loss of profit will ordinarily take into account the pieces of evidence produced by the parties, the underlying facts and economic outcome of the harmful conduct.

The methodology of assessment in each case, however, may differ in view of the underlying matter, type of contract and circumstance of the harmful act or contractual breach. In most of the cases, the methodology will be related to economic, accountant, environmental, engineering and medical assessments.

For example, company A hires company B to perform the construction of a certain facility to produce an important product of its portfolio. In view of company B's complete

default towards the contract, company A will be entitled to claim for (1) reimbursement of the expenses it incurred to hire a third company to perform the construction, and (2) the loss of profit it suffered due to a delay in producing the goods. In this hypothetical case, the assessment of the damage will take into account the actual amount that company A has spent and paid to third parties to remediate company B's default (accountant examination) and the foreseeable, reasonable gains that company A would have obtained if it had started producing the goods within the expected time (economic and accountant examination).

vi Discount rates

As a general rule, there is no limitation in value for the amount of indemnification for compensatory damages and loss of profit, as it must correspond to the exact amount of losses suffered by the injured party, compensating it as if the harmful act had never occurred (Brazilian Civil Code, Article 945). When assessing the losses, the expert may take into account certain circumstances of the case, such as parties' concurrent default, plaintiff's negligence, economic environment aggravating the loss, etc., which must be evidenced by the parties during the lawsuit.

vii Currency conversion

The amount of indemnification resulting from moral damage or damage to property (compensatory damages and loss of profit) will be assessed by the court in Brazilian reais.

Note that the case law recognises contracts stipulating amounts to be paid in currency other than reais as valid, provided that the payment is made in Brazil upon the conversion of the amount into reais according to the exchange rate of the date of payment.² In the case of claims for damages based on foreign amounts set forth in such contracts, the same rule will apply and the payment of the indemnification will be made in reais. In the case of decisions rendered by foreign courts, the amount fixed in foreign currency may also be enforced in Brazil upon conversion into reais, if the decision is previously recognised by the Superior Court of Justice.³

viii Interest on damages

If the claim is based on a contractual breach, the amount of the indemnification assessed by the court-appointed expert will accrue interest counted from the date on which the defendant was served with process, as well as inflation from the date of the decision confirming the amount of the indemnification or from the date of the contractual breach, depending on the underlying discussion. On the other hand, if the claim is based on a civil wrong arising from an act or omission independently of a contract (tort), the indemnification amount will accrue interest counted from the date of the harmful conduct, and will be subject to inflation from the date of the decision confirming the amount of the indemnification.

2 AgInt nos EDcl no AREsp 1049346/GO, Superior Court of Justice.

3 SEC 11969/EX, Superior Court of Justice.

The Brazilian Civil Code, Article 406,⁴ sets forth that, when the parties have not agreed on the default interest, it will be calculated considering the same index accruing over defaulted taxes payable to the National Treasury.

There is a discussion on whether the index to be considered for the purpose of Article 406 would be the Special Settlement and Custody System (SELIC), which already comprehends interest and inflation and is decided by the Monetary Policy Committee, or 1 per cent per month, which may be coupled with inflation. The Superior Court of Justice has ruled that, unless the decision expressly decides otherwise, the SELIC index will be considered for the purpose of Article 406 of the Brazilian Civil Code. However, the courts in Brazil have ordinarily ruled that the interest should be set at the threshold of 1 per cent per month plus inflation – in these cases, because there was an express court decision on the matter, the 1 per cent interest rate would prevail over the SELIC index for that specific case.

ix Costs

The fees and expenses involved in the production of expert examination aiming to assessing damage to property (to claim compensatory damages and loss of profit) may vary depending on the scope and complexity of the assessment. As a general rule, each party will pay the fees of the assistant expert they have appointed, whereas the fees of the court-appointed expert will be paid by the party that has requested the expert investigation, or else shared when the expert investigation is ordered *ex officio* by the court or requested by both parties (Brazilian Code of Civil Procedure, Article 95). The defeated party will be ordered to reimburse such costs to the winning party.

x Tax

Amounts paid to the injured party as moral damages or damages to property are generally not subject to income tax, as they do not represent a gain, but merely compensate the losses suffered by the injured party. However, a specific analysis may be needed to confirm the incidence of any other tax over the amount of the indemnification, in view of the circumstances of each case and of the companies and individuals involved.

III EXPERT EVIDENCE

i Introduction

The Brazilian Code of Civil Procedures (Federal Law No. 13,105/2015) sets forth general provisions on evidentiary phase in civil lawsuits. Each party has the burden to prove its own allegations and claims through any sort of evidence available, such as documents, expert examination, witnesses and depositions (Code of Civil Procedures, Articles 369 and 373).

When it comes to expert evidence, the court may confirm the need of producing the expert examination depending on the facts, claims and circumstances of each case. The expert examination may be denied if (1) the confirmation of the fact does not depend on specific technical knowledge, (2) it is unnecessary in view of other pieces of evidence already produced, especially documents, and (3) the production of expert examination is impracticable.

⁴ Brazilian Civil Code, Article 406: When there have been no contractual provisions on default interest, or if no rate has been stipulated for default interest, or when default interest arises from legal determination, it shall be set at the rate then accruing on past-due tax obligations payable to the National Treasury.

Unlike other jurisdictions, the Brazilian legislation does not provide for a broad discovery of documents allowing the party to oblige its opponent to disclose a vast number of documents and information as evidence in the litigation. Normally, the parties must rely on their own pieces of evidence, use them to substantiate the claims raised in the lawsuit and, then, submit such evidence to scrutiny by the counterparty and by the court (adversarial principle). However, if a certain document is necessary for the expert examination, the court may order the party to disclose it in court. In order to substantiate this request for disclosure, the party must satisfy certain legal requirements – such as to evidence that it does not have access to all relevant documents needed to prove its injury, to evidence with a high level of certainty that the documents exist, are in possession of the counterparty or third party, as well as the purpose of the document and their relevance for the matter under scrutiny.

ii The role of expert evidence in calculation of damages

When it comes to lawsuits involving damages, the evidentiary phase is a necessary step for a decision on the merits. As the Brazilian Civil Code links the duty to indemnify to the proof of fault or wrongful misconduct, as well as to the extension of the damages, the plaintiff shall produce all pieces of evidence needed to confirm the concrete occurrence of the damage and its actual extension in order to obtain a favourable decision on the merits.

It is technically possible for the plaintiff to allege that an illegal act performed by the defendant has caused losses (i.e., evidencing, at least with minimal grounds, that the losses it is claiming indemnification for actually occurred and caused concrete damage), but stating that the extent or amount of such losses will be assessed during the expert examination phase or after the *res judicata* through a liquidation phase. In other words, the plaintiff must evidence that such losses have occurred concretely and have caused or are causing damage, but the work of experts appointed by the court is needed to confirm the exact extent of the losses.

iii The court's role excluding and managing expert evidence

Considering the factual background of the dispute, and given the fact that the evidence is directed to the judge's scrutiny, the judge is empowered to delineate the elements of the case and to determine, independently of parties' request, which pieces of evidence should be produced in order to enable the rendering of a decision on the merits (Code of Civil Procedures, Article 370). In other words, as the judge is the final addressee of the evidence and has the duty to review it in order to issue a decision, he or she must order the evidentiary phase. The judge also has discretion to analyse the pieces of evidence attached to the case files to confirm whether additional pieces of evidence are necessary for a more accurate decision on the merits.

The pieces of evidence to be produced in suits for damages would depend on a case-by-case review, as the factual background of the dispute is relevant for the definition of the award and indemnification values.

There is no restriction on the types of evidence to be produced in a civil lawsuit. Although the Code of Civil Procedures contains indication of certain types of evidence that may be produced (i.e., documents, expert examination and witnesses) the list is considered merely indicative, allowing the parties to request the production of other pieces of evidence, provided that they are not illegal or against the moral standards.

There are specific provisions to be followed in the evidentiary phase. For instance, the parties are obliged to present with the complaint and with the defence all documents related

to their allegations and claims. New documents may be attached to the case files in response to other party's allegation or in case the party is able to evidence that a document was not available or did not exist by the time of the filing of the complaint or defence.

As a general rule, each party is equally obliged to prove its own allegations and claims raised in the complaint and in the defence. In exceptional cases, the court may impose on the counterparty the burden to produce certain pieces of evidence important for the matter under scrutiny, dynamically allocating the burden of proof among the parties. For instance, in view of the peculiarities of the lawsuit, this inversion on the burden of proof may occur when (1) the party originally obliged to produce the evidence in court cannot do so, or (2) one of the parties has more ready access to the evidence. Such decision shall be properly justified and the inversion cannot take place in cases where the imposition results in an obligation impossible to be complied with (Code of Civil Procedures, Article 373, Sections 1 and 2). This dynamic distribution of the burden of proof may also be agreed by the parties, before or during the lawsuit, as the Code of Civil Procedures allows the parties to allocate the burden of proof by themselves, except in cases of inalienable rights or when the exercise of a right by one of the parties may become extremely difficult.

iv Independence of experts

If the court confirms the need to produce an expert examination, considering the facts, claims and circumstances of the case, it will appoint an expert with technical knowledge and expertise on the matter to conduct the examination. At the same time, the court will summon the parties to appoint their own experts to assist in the works and to submit queries to the expert in order to guide the technical examination.

Like the judge himself or herself, the court-appointed expert must be an independent and impartial character in the lawsuit, solely intended to guide the judge in the analysis of the technical aspects of the underlying matter. Thus, the court-appointed expert will have the same duty of impartiality and independence and will be subject to the same rules of impediment, bias and disqualification that apply to judges (Code of Civil Procedures, Article 465, Section 1, I). The expert assistants appointed by the parties, on the other hand, are not subject to the duty of impartiality – they will represent the parties and their counsels, from a technical point of view, in supervising and assisting the production of evidence.

The expert is generally appointed by the judge from a list of names of people enrolled in the courts' registries. The Code of Civil Procedures, however, allows the parties the possibility of agreeing on names (on a single name or on a list of names) of experts to be possibly appointed by the court. This possibility is especially important in high-profile, complex cases, where parties would be able to suggest renowned names with profound expertise and background in the field of knowledge needed to an accurate solution of the matters under scrutiny. Note, however, that the judge is not bound to the parties' joint submission of name. Even if the judge agrees and confirms one of the names jointly submitted by the parties, this expert will be appointed by the court and, therefore, will be subject to the duty of impartiality.

v Challenging experts' credentials

The parties are allowed to challenge the expert's credentials within 15 business days counted from court appointment.

In this sense, the parties will be able to sustain not only that the court-appointed expert does not have the necessary technical expertise to perform the technical examination, considering the field of knowledge demanded by the facts, claims and circumstances of the

case, but also submit requests and present pieces of evidence to disqualify the expert owing to impediment and bias. The court will decide on the parties' challenges to the court-appointed expert (Code of Civil Procedures, Articles 465, Section 1, I, and 468, I and II).

vi Novel science and methods

The parties are allowed to produce any type of piece of evidence to prove their claims and allegations, as long as the intended evidence is not illegal or against moral standards. The same applies to novel science and methods: the party may request the use of novel science and methods in order to prove its claims and allegations. The court will decide whether the method may be used, considering the underlying facts and the circumstances of the case.

vii Oral and written submissions

The court-appointed expert will submit a written report containing at least (1) a summary of the technical aspects of the case, (2) the analysis conducted with the help of the parties' expert assistants, (3) the indication of the method used in the examination, (4) the responses to the parties' queries, and (5) the conclusion on the technical matters under discussion. The parties and their expert assistants will be able to scrutinise the court-appointed expert's report, agreeing or disagreeing with it, totally or partially, or to request clarification or additional analysis, submitting additional queries to complement certain incomplete or inaccurate aspects of the examination.

The party may also request the court to summon the court-appointed expert to attend a hearing in order to clarify some aspects of the technical examination. In this case, the parties must submit questions intended to be answered by the expert in such hearing.

In cases of low complexity, instead of ordering the production of a thorough expert examination, the court may just question (orally) a professional with expertise on the matter in order to obtain information and clarification needed for the merits of the case (Code of Civil Procedures, Article 464, Section 4 and 5).

IV RECENT CASE LAW

The general requirements for imposition of the duty to redress damage (fault or misconduct, chain of causation and damage), as well as the extension of the damage, are the main matters under dispute in cases involving a claim for damages. Even though the case law has been developing on the matter since 1916, with the revoked Civil Code, the disputes involving claims for damages, especially when it comes to the legal requirements for assessing the indemnification, remains challenging.

In a recent decision rendered in a dispute involving damage arising from breach of contract and expectations among the parties, the Fourth Chamber of the Superior Court of Justice decided that oral agreement on supplying of machinery shall be considered valid for the purpose of verifying the duty to pay indemnification for breach of contractual obligations. According to such decision, once the hired party has evidenced in an expert examination that it has suffered losses owing to the production of materials that the other party promised to acquire, failing to comply with the oral agreement is sufficient for the imposition of the duty to indemnify, based on the violation of the good faith inherent to contractual obligations. The court sentenced the party to indemnify the counterparty for loss of profits and actual damage, owing to evidence of investments performed by such party to comply with the expectation of sale deriving from the oral agreement. The decision also stated that the judge

is empowered to analyse the expert evidence produced in the case files and is not bound to the analysis conducted by the court-appointed expert, even though his or her report is relevant for the decision on the merits of the case.⁵

It is worth highlighting that class actions in Brazil are usually filed to defend collective rights for which different types of civil liability are applicable. Since the consumer and environmental laws set forth that the civil liabilities in such matters shall be considered joint and several, there are no discussions on actual fault or misconduct to evidence the duty to redress the damage. Consequently, in those cases, the courts tend to provide a broad interpretation of general civil concepts applicable to civil liability, amplifying the responsible parties on consumer and environmental cases. An example of such broad understanding are the discussions related to requirements for piercing the corporate veil to impose liabilities on shareholders when the responsible party has no asset to redress the damage. In a decision that is considered a relevant precedent on the matter, the Superior Court of Justice states that piercing the corporate veil is applicable whenever the legal entity responsible for the damage – either to consumers' collective rights or to the environment – does not have enough assets or financial conditions to repair the damage, depending only on evidence of insolvency of the legal entity that had caused the damage.⁶

There are also cases where some of the requirements for imposition of the duty to redress civil damage were mitigated in court. In a discussion involving infringement of trademark protection, the Third Chamber of the Superior Court of Justice decided that sentencing the violating party to indemnify damage deriving from the infringement of trademark rights does not depend on evidence of loss. According to the decision, the violation of trademark rights is sufficient to sentence the offender to indemnify the injured party, since it is assumed that such violation causes losses to the injured party. The main justification of the decision is that evidence of actual and substantial damage deriving from the infringement of trademark rights is extremely difficult to procure, owing to the nature of trademark rights; thus, losses shall be assumed as proven based solely on evidence of infringement of trademark rights.⁷

5 Special Appeal 1.309.972/SP, 4th Chamber, Reporting Justice Luis Felipe Salomão, decided on 27 April 2017.

6 Special Appeal 279.273/SP, 3rd Chamber, Reporting Justice Nancy Andrighi, decided on 4 December 2003.

7 Special Appeal 1.309.972/SP, 3rd Chamber, Reporting Justice Nancy Andrighi, decided on 6 April 2017.

CANADA

*Junior Sirivar and Andrew Kalamut*¹

I OVERVIEW

In Canada, damages are awarded to successful parties for their pecuniary and non-pecuniary losses. Non-pecuniary losses generally include pain and suffering or mental distress. A pecuniary loss generally includes losses that can be measured in a monetary sum, arising from loss of property, loss of services, personal injuries, loss of reputation or money, and damage to economic interest. This chapter will primarily focus on Canadian compensatory damages for pecuniary losses that are caused by breaches in Canadian contract or tort law.

The fundamental principle underlying Canadian private law remedies is *restitutio in integrum*, meaning ‘restoration to original condition’.² Private law damages arising from tort or contractual breaches are meant to be compensatory in nature. The award aims to restore a successful plaintiff to the position it occupied before the legal wrong occurred.³ Further, compensatory damages do not seek to punish the defendant.⁴ There is also an emphasis in Canadian law that damages awards should always be consistent, fair and rational.⁵ These principles have informed many, if not all, of the aspects comprising the law of damages in Canada.

Non-compensatory damages, while available in Canada, apply only in certain circumstances where the facts of the case and the defendant’s conduct require it.⁶ For example, exemplary, nominal, punitive and restitutionary damages fall under the umbrella of non-compensatory damages. If equitable principles are found to apply, then monetary relief may be available by way of equitable damages that compensate for losses where a legal common law award would be insufficient.⁷

1 Junior Sirivar is a partner and Andrew Kalamut is an associate at McCarthy Tétrault LLP. With assistance from Bonnie Greenaway, student-at-law.

2 2105582 *Ontario Ltd. (Performance Plus Golf Academy) v. 375445 Ontario Limited (Hydeaway Golf Club)*, 2017 ONCA 980 at para. 58 (CanLII) [*Performance Plus*]; citing *Milina v. Bartsch* (1985), 49 B.C.L.R. (2d) 33 at p. 78, 1985 CanLII 179 (BC SC), *McLachlin J. (as she then was)*; *Barber v. Vrozos*, 2010 ONCA 570 at para. 86 (CanLII); *Rougemont Capital Inc. v. Computer Associates International Inc.*, 2016 ONCA 847 (CanLII), at para. 44 (CanLII) [*Rougemount*].

3 S.M. Waddams, *The Law of Damages* (Carswell: 2018) (loose-leaf, online version) at ch. 1.10 [Waddams].

4 *Performance Plus*, note 2 at para. 58.

5 *Andrews v. Grand & Toy Alberta Ltd.*, [1978] 2 S.C.R. 229 at p. 230, 1978 CanLII 1 (SCC) [Andrews].

6 *Performance Plus*, note 2 at para. 60.

7 Jeffrey Berryman, *Remedies: Cases and Materials* (Toronto: Emond Montgomery Publications, 2012) at p. 1038.

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

Generally, Canadian courts quantify financial loss and assess damages by valuing what the plaintiff's position would have been 'but for' the defendant's wrong.⁸ A successful plaintiff is awarded monetary damages to replace its loss; and, if applicable, its lost opportunity, income, or profit that it would have otherwise earned.⁹

ii Evidence

In some cases, it is not always clear what the value of the plaintiff's loss is. Once liability is established, a plaintiff has the onus of proving its damages with cogent fact and expert evidence.

Canadian law recognises that the evidence available in a particular case may not precisely quantify the damages award. In these cases, although the plaintiff still bears the onus to prove the facts upon which damages are estimated, the difficulty in quantifying damages does not bar the court from awarding damages. A liable defendant is never excused from paying damages because of evidentiary flaws, so long as there is some evidence upon which a court can draw facts to appropriately quantify the loss.¹⁰

In cases involving breach of contract, the contract may provide the best evidence of the plaintiff's financial loss. Where a contract has not provided for the value of the agreement as a whole or certain terms, the court will determine value by the market price of the goods or services offered.¹¹

iii Date of assessment

The date of assessment for damages is context specific and depends on the wrong that has been perpetrated. The following is an overview of the general principles that guide how the date of assessment is determined in certain instances.

Absent special circumstances, the appropriate date to assess damages for breach of contract or a tort is at the date of the breach.¹² Although there are exceptions to this where fairness requires it, the presumption is not easily displaced.¹³ Canadian law focuses on the early crystallisation for dates of assessment, for the following reasons.

An early crystallisation of the plaintiff's damages promotes efficient behaviour: the litigants become as free as possible to conduct their affairs as they see fit. Early crystallisation also avoids speculation: the plaintiff is precluded from speculating at the defendant's expense by reaping the benefits of an increase in the value of the goods in question without bearing any risk of loss.¹⁴

The date of assessment is most commonly disputed when the property that the plaintiff was deprived of has changed in value between the date of the breach and the date of the

8 Waddams, note 3 at ch. 1.30.

9 *ibid* at ch. 1.10.

10 *Borrelli v. Chan*, 2018 ONSC 1429 at para. 942 (CanLII) [*Borrelli*].

11 Waddams, note 3 at ch. 1.660.

12 *Rougemount*, note 2 at paras. 45, 47 and 50; Waddams, note 3 at ch. 2.270; *Asamera Oil Corp. Ltd. v. Sea Oil & General Corp.*, [1979] 1 S.C.R. 663 at pp. 664-65, 1978 CanLII 16 (SCC) [*Asamera Oil*].

13 *Rougemount*, note 2 at para. 50;

14 *Kinbauri Gold Corp. v. Iamgold International African Mining Gold Corp.*, [2004] 246 D.L.R. (4th) 595 at para. 125, 2004 CanLII 36051 (ONCA) [*Kinbauri*].

judgment. This commonly occurs in the context of speculative property, such as shares or other ownership interests in corporations or real estate. If the value of the property in issue has declined during the period leading to trial, the plaintiff is advantaged by the damages being assessed at the date of the breach. For example, consider that a plaintiff enters into an agreement to purchase property for C\$1000, and the defendant then breaches the contract. At the trial, the property is worth only C\$500. If damages are awarded as assessed on the date of the breach, the plaintiff will receive double the present value of the property. Such an outcome is often criticised as violating the fundamental principle of damages that the plaintiff is not to be put in a better position.¹⁵ On the other hand, if the value of the property increases between the date of the wrong and the date of the judgment, the defendant benefits.

If the fluctuation in value would violate principles of equity or would work an unfairness on either party, Canadian courts may exercise their discretion and alter the date of assessment. Canadian courts have done so where no market exists to replace undelivered shares at the date of breach¹⁶ or in relation to speculative property, including shares, whose value is subject to sudden and constant fluctuations of unpredictable amplitude.¹⁷

iv Financial projections

Financial projections are often used to assist the court in quantifying the correct damages award for a prospective loss. For example, financial projections are often used in the context of quantifying future losses from income or profit from a business. Although financial projections may be used to assist in quantifying a plaintiff's loss, Canadian courts recognise that calculating damages is not a precise science.¹⁸ The court has wide discretion to draw its own inferences from the facts to determine what a reasonable projection of the future loss is.

Expert evidence is typically required to prepare a financial projection. The methodology used to provide the financial projection is of critical importance. Soundly calculated projections will be given more weight by the court.¹⁹

Although it is ultimately up to the expert and the party's counsel to determine what methodology is to be used, it should aim to be as realistic as possible.²⁰ For example, where a contract has alternative modes of performance, then the financial projection should ensure it adopts or provides for the Canadian presumption the defendant would have performed the contract in the way that is least burdensome to it.²¹ Second, the financial projection should be based on objective facts known at the time of the loss, rather than hypotheticals or information that was obtained with the benefit of hindsight.²² This is in line with the general Canadian principles that damages ought to be reasonable and not overcompensate the plaintiff.

15 Waddams, note 3 at ch. 1.660.

16 *Kinbaouri*, note 14 at para. 126.

17 *Asamera Oil*, note 12 at pp. 664-65.

18 *AgribRANDS Purina Canada Inc. v. Kasamekas*, 2011 ONCA 460 at paras. 56,68 (CanLII).

19 *ibid* at paras. 44-70; Expert evidence is discussed in full, below.

20 For a full discussion regarding expert methodology, see Farley J. Cohen & Prem M. Lobo, 'Business value as a measure of loss in litigation contexts: reflecting business 'reality' over hypothetical 'fantasy' (2011) *Adv J* [Cohen & Lobo].

21 *Hamilton v. Open Bakery*, 2004 SCC 9 at para. 20 (CanLII).

22 *Ford Motor Company of Canada, Ltd. v. Ontario Municipal Employees Retirement Board*, 79 O.R. (3d) at paras. 38-40, 2006 CanLII 15 (ONCA).

v Assumptions

In a similar vein to financial projections, assumptions are a necessary and important element in the quantification of prospective losses such as future income, care, financial loss and business.

It is common in Canada for a party to clearly outline the key assumptions a valuator has made in its written expert report. The basis of the valuator's conclusions ought to be clearly understood if the court is to base its damages award on the report.²³

Parties can offer damages reports containing different assumptions and calculations to allow the court to assess a number of options.²⁴ Canadian courts are free to accept or reject the assumptions that underlie the party's submission quantifying their damages. To challenge the quantification of a damages assessment, the party may critique the assumptions made by another party in their submitted damages calculation. The assumption that is to be accepted by the court ought to be reasonably supported by the evidence and the facts of the case.²⁵

vi Discount rates

Discount rates are applied to Canadian judgments to account for the fact that money may be paid in advance of when it otherwise would have been owing, thus generating interest that would otherwise not have been and will be earned.²⁶ The discount rate reflects the rate of interest that the award of damages will earn, the effect of inflation and the effect of income taxes on the award, known as the time value of money.

In Canada, the regimes in various provinces and territories differ on whether the discount rate is legislated or if the rate is determined by the court having heard the evidence. Where imposed by legislation, evidence may be led to rebut the statutory discount rate.

The following table outlines the current discount rates that apply to each province or territory.

Discount rates applicable for tort cases across the country	Item of pecuniary loss	Source	Discount rate
British Columbia	Future care	Law and Equity Act, at Section 56(2)(b), BC Reg 352/81	2%
	Future wage loss	Law and Equity Act, at Section 56(2)(a), BC Reg 352/81	1.5%
Alberta	Future care and wage loss	No mandatory discount rate	
Saskatchewan	Future care and wage loss	Queen's Bench Rules, at Section 284B(1)(b)	3%
Manitoba	Future care and wage loss	Court of Queen's Bench Act, at Sections 83(1) and 83(2)	3%
Ontario	Future pecuniary loss	Rules of Civil Procedure, RSO 1990, c C-43 at Section 53.09 (Ontario Rules of Civil Procedure)	0% for first 15 years, 2.5% thereafter for any later period covered by the award

²³ Cohen & Lobo, note 20.

²⁴ *Schenker v. Scott*, 2014 BCCA 203 at para. 72 (CanLII) [Schenker]; *El-Khodr v. Lackie*, 2017 ONCA 716 at para. 9 (CanLII),

²⁵ *IBM Canada Limited v. Waterman*, 2013 SCC 70 at paras. 90-91 (CanLII); *Schenker*, note 24 at para. 76; *Hallatt v. The Queen*, 2001 CanLII 590 at para. 30; [2001] 1 C.T.C. 2626.

²⁶ Waddams, note 3 at ch. 3.990.

Discount rates applicable for tort cases across the country	Item of pecuniary loss	Source	Discount rate
Quebec	Future wage loss	Civil Code , Regulation under Article 1614	2%
	Other future pecuniary loss		3.25%
New Brunswick	Future pecuniary loss	Rules of Court, N.B. Reg. 82-73, at Section 54.10(2)	2.5%
Nova Scotia	Future pecuniary loss, other than loss of business income	Civil Procedure Rules, at Section 70.06(1)	2.5%
	Future loss of business income	Civil Procedure Rules, at Section 70.06(2)	A party may prove a discount rate to be used in calculating the difference between estimated investment and price inflation rates for calculating the value of damages for future loss of business income
Prince Edward Island	Future pecuniary loss	Rules of Civil Procedure, at Section 53.09(1)	2.5%
Newfoundland and Labrador	Future pecuniary loss		No mandatory discount rate
Northwest Territories	Future pecuniary loss	Judicature Act, R.S.N.W.T. 1988, c. J-1, at Section 57(1)	2.5%
Nunavut	Future pecuniary loss	Judicature Act, S.N.W.T. 1998, c. J-1, at Section 56(1)	2.5%
Yukon	Future pecuniary loss	No mandatory discount rate	

vii Currency conversion

The Canadian Currency Act²⁷ requires that any monetary award in a legal proceeding in Canada be stated in Canadian currency. As a result, many Canadian courts convert awards for loss into Canadian dollars, even if the loss stems from a foreign currency.

Since the date of the assessment of damages is typically the date of breach, fluctuations in foreign exchange rates between the date of the breach and the trial date can become an issue in cross-border litigation. For example, if a plaintiff is wronged and commences an action to recover judgment to satisfy US currency, and the value of the Canadian dollar decreases between the date of the wrong and the date of the trial, the defendant benefits as fewer US dollars will be required to satisfy the judgment. In the past, Canadian jurisprudence has stubbornly clung to the date of the breach for the currency conversion.²⁸ However, some provincial jurisdictions, such as Ontario and British Columbia, have statutorily prescribed that the currency conversion occurs on the date of judgment.

Courts typically recognise that a plaintiff should be subjected to the risk of a fluctuating exchange rate.²⁹ For example, in the British Columbia Supreme Court decision of *Naturex Inc. v. United Naturals Inc.*, United Naturals had contracted to have Naturex deliver plant extract products.³⁰ The shipments were payable in US dollars. When United Naturals stopped paying Naturex, Naturex sued to recover US\$248,000 from United Naturals. Between the

27 R.S.C., 1985, c. C-52, s.12.

28 *Gatineau Power Co. v. Crown Life Insurance Co.*, [1945] S.C.R. 655 at p. 657, 1945 CanLII 33 (SCC); *Batavia Times Publishing Co., v. Davis*, (1978), 20 O.R. (2d) 437 (HC), aff'd (1979), 26 O.R. (2d) 249 and 800n (CA).

29 *Wei v. Mei*, 2018 BCSC 1057 at para. 54 (CanLII),

30 *Naturex Inc. v. United Naturals Inc.*, 2016 BCSC 1502 at para. 21 (CanLII).

date the tort occurred and the claim was commenced, the value of the Canadian dollar fell against the US dollar. Unless adjusted, on the date of judgment, United Naturals would have received a 'windfall', as it would require far fewer US dollars to pay the judgment in Canadian dollars.³¹ The court held that the most appropriate date upon which to order the conversion calculation was the date the claim was actually commenced.

viii Interest on damages

In Canada, pre-judgment interest is typically added to a damages award to acknowledge that if a cause of action arises, and the wronged party waits for years to receive its judgment, the wronged party has been dealt two wrongs.³² Accordingly, pre-judgment interest is typically calculated from the day the cause of action arose to the date of the judgment.

Post-judgment interest may also apply to damages awards to account for the period of time between the date of the judgment and the date of actual payment.³³

The application and calculation of interest rates may be provided by the agreement between the parties, which the court will likely uphold.³⁴ For example, the Ontario Superior Court of Justice recently upheld a post-judgment interest rate of 24 per cent.³⁵ Although the Court noted this appeared to be 'excessive', it held it was necessary to enforce this clause in order to uphold the principle of freedom of contract between parties.³⁶

The applicable statutory regimes govern where there is no agreement, or where the agreement is silent as to interest rates. Legislation from each provincial or territorial jurisdiction within Canada permits or requires the court to award interest on monetary judgments, and provides the applicable rates.³⁷ Some provinces specify the rate to be applied, but the court is free in all provinces to award interest at commercial rates.³⁸ Although the courts retain their discretionary power to adjust the amount of interest that is payable under statute, the legislation in each jurisdiction contains different language, which may limit how a court exercises its discretion.³⁹

Parties should therefore be mindful of the legislation in each province or territory which both specifies a party's entitlement to interest and may impose limits on whether a court will deviate from the interest award under statute.

31 *ibid.*

32 Waddams, note 3 at ch. 7.330.

33 Waddams, note 3 at ch. 7.1000.

34 *241 Pizza (2006) Ltd. v. Loza*, 2017 ONSC 4171 at paras. 16-17 (CanLII).

35 *ibid.*

36 *ibid* at para. 16.

37 Judgment Interest Act (Alta.); Court Order Interest Act (B.C.); Court of Queen's Bench Act (Man.); Judicature Act (N.B.), Section 45; Judgment Interest Act (Nfld. & Lab.); Judicature Act (N.W.T.), Sections 55, 56, 56.1, 56.2; Judicature Act (N.S.), Section 41; Courts of Justice Act (Ont.), Sections 127-8; Judicature Act (P.E.I.), Sections 56-60; Pre-judgment Interest Act (Sask.). Also see Waldron, *The Law of Interest in Canada* (Toronto, Carswell, 1992) at pp. 131-59.

38 Waddams, note 3 at ch. 7.470. See Ontario, for example, which sets out the applicable interest rate in the Courts of Justice Act, RSO 1990, c. C. 43 at Section 127(1).

39 See *Bank of America Canada v. Mutual Trust Co.*, 2002 SCC 42 (CanLII). In that case, the Supreme Court of Canada held, despite Ontario's Courts of Justice Act, compound interest could be awarded in some circumstances at common law.

ix Costs

The well-established principle in Canadian law is that costs of the litigation follow the result.⁴⁰ This means that, generally, the successful party to the litigation is awarded its costs of the action for damages, subject to exceptional circumstances that require the court to exercise its discretion.⁴¹

Costs are typically awarded on a partial indemnity scale, which often amounts to less than 50 per cent of actual costs. Costs may be awarded on an elevated scale in exceptional circumstances. For example, if a party has engaged in conduct during the course of litigation that is worthy of rebuke from the court, such as tactical motions to delay the disposition of the matter, the scale of costs may be adjusted.⁴²

In all cases, costs awards must be fair and reasonable in the circumstances.⁴³ To give effect to this principle, the court may find that a different costs award is appropriate from what is specified in the legislation.⁴⁴

x Tax

The quantification of the damages award

In Canadian law, there is no deduction to the plaintiff's damages award for the income tax that would have been paid on a compensatory award for lost income, earnings, or profit.⁴⁵ Canadian law rejects that the defendant can reduce the amount of damages owed to the plaintiff on the grounds of applicable taxes. Canadian courts have referred the question of how to tax damages awards to the Canadian legislature as a matter of tax policy.⁴⁶

In very limited circumstances, a tax benefit may reduce a damages award where it is found that 'but for the loss', the plaintiff would otherwise not have received tax benefit.⁴⁷ This is only where sufficient evidence is led to specifically calculate the tax benefit and it is not merely hypothetical.⁴⁸

The taxation of the damages award

Once the plaintiff has received a damages award, how the award is taxed under Canada's Income Tax Act (ITA), from either the payor or payee's perspective, depends on how the award is characterised with reference to the provisions under the ITA and the existing jurisprudence,

40 For a full discussion, see Mark M. Orkin, *The Law of Costs*, 2ed (Aurora, Ontario: Canada Law Book, 2015) (Carswell: 2018) at ch. 205.2 [Orkin].

41 For example, see Ontario's Courts of Justice Act, RSO 1990, c. C-43, at Section 131(1); Rules of Civil Procedure, RSO 1990, c. C-43, at Section 57.01(1). In *The Law of Costs*, Orkin has also classified several categorical exceptions to the general rule that costs follow the result, following the case of *Cooper v. Whittingham*: (1) misconduct of the parties; (2) miscarriage in the procedure; (3) oppressive and vexatious conduct of the proceedings; and (4) other cases.

42 Orkin, note 40 at ch. 205.2

43 *Boucher et al. v. Public Accountants Council for the Province of Ontario et al.*, 2004 CanLII 14579 at paras. 24, 71 O.R. (3d) 291 (ONCA).

44 *ibid.*

45 *The Queen in Right of Ontario v. Jennings*, [1966] S.C.R. 532 at p. 541, 966 CarswellOnt 61; *Cunningham v. Wheeler*; *Cooper v. Miller*; *Shanks v. McNee*, [1994] 1 S.C.R. 359 at pp. 417-18, 1994 CanLII 120 [Cunningham].

46 *Cunningham*, note 44 ; Waddams, note 3 at ch. 3.950.

47 *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377 at p. 399, 1994 CanLII 70.

48 *ibid.*

if any.⁴⁹ Although the jurisprudence in this area is not always clear, general rules have emerged that can assist counsel in determining the tax liability that may arise from a damages award. Counsel must carefully scrutinise what type of damages award is being received.

Under the ITA, a taxpayer is liable to pay tax on any income arising from the non-exhaustive ‘source’ listed in the ITA, which is income from office, employment, business and property, or any other provision under the ITA that may give rise to tax liability.⁵⁰ Further, the damages award may be taxable if it is compensation for taxable income under the ITA.⁵¹ If the award is compensation for a non-taxable capital receipt, then it is likely not taxable.⁵²

Based on these principles, it is clear that if the damages award can reasonably be considered to be income that would otherwise be taxable under the ITA then it is taxable in the hands of the recipient.⁵³ For example, the compensation for a finder’s fee, loss of profits, or disability insurance benefits in arrears have all been held to be taxable as income.⁵⁴ A payment for damaged or destroyed property is treated as a taxable capital receipt that would otherwise have been received had the property been sold.⁵⁵ Punitive damages are considered to be ‘windfalls’ that are non-taxable.⁵⁶

Damage awards for personal injury claims are treated differently. All amounts that qualify as pecuniary special or general damages are excluded from taxable income regardless of the fact that the amount of such damages may have been determined with reference to loss of earnings of the taxpayer.⁵⁷

From the payer’s perspective, as a general rule, a damages payment and related costs will be deductible if incurred for the purpose of earning, producing or protecting business income; acquiring or protecting a capital asset.⁵⁸

III EXPERT EVIDENCE

i Introduction

The use of expert evidence is an exception to the ‘opinion rule’ established in Canadian common law that requires a witness to testify to facts gained from their senses.⁵⁹ In addition

49 R.S.C., 1985, c. 1 (5th Supp) [ITA]; *Schwartz v. Canada*, [1996] 1 SCR 254 at para 52, 1996 CanLII 217 [Schwartz]

50 ITA, note 49 at Section 3.

51 See Canada Revenue Agency, Interpretation Bulletin IT-365R2, ‘Damages, Settlements and Similar Receipts’ online: <https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/it365r2/archived-damages-settlements-similar-receipts.html>. [Bulletin IT-365R2].

52 Windfalls, such as lottery winnings, inherited amounts, gifts and other gratuitous payments are not taxable because they lack the essential elements of ‘income’. See David Wentzell, ‘Taxation of Income from Unlisted Sources: An Analysis of *Schwartz v. The Queen*’, Report of Proceedings of Forty-Eighth Tax Conference, 1996 Tax Conference (Toronto: Canadian Tax Foundation, 1997), 67:1-15.

53 Bulletin IT-365R2, note 51; *Schwartz*, note 48 at para. 52.

54 CED 4th (online), Income Tax, ‘Damages and Settlements’ at (IV.7.(a)) Section 301 [CED].

55 *ibid.*

56 *Bellingham v. R.*, [1996] 1 C.T.C. 187 at paras. 2, 46, 1995 CarswellNat 881 (FCA) [*Bellingham*].

57 Bulletin IT-365R2, note 50; *Bellingham*, note 55 at para. 45; CED, note 54 at (IV.7.(b)) Section 303.

58 See Canada Revenue Agency, Interpretation Bulletin IT-467R2 ‘Damages, Settlements and Similar Receipts’ online: <https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/it467r2/archived-damages-settlements-similar-payments.html>.

59 Gordon D. Cudmore, *Civil Evidence Handbook* (Carswell: 2018) (loose-leaf, online version) at ch. 14.1 [Cudmore].

to the principles discussed below, Canadian jurisdictions have legislated procedural preconditions that must be complied with in order for written and oral expert evidence to be admitted at trial.⁶⁰

ii The role of expert evidence in calculation of damages

Expert witnesses are frequently retained in commercial and personal injury matters to assist the court in quantifying the plaintiff's loss. The purpose of expert evidence is to assist the court to understand the evidence regarding the party's loss so that the court can reach the correct damages award.

For example, accounting, financial or valuation experts are frequently called upon by parties to assist the court in the quantification of damages.⁶¹ In particular, courts routinely admit expert evidence in cases where the quantification of a financial loss or business value is complex, involves a significant dollar amount, or is in dispute between the parties.⁶²

iii The court's role excluding and managing expert evidence

Admission of expert evidence for a damages assessment depends on whether it meets the following basic criteria established by the Supreme Court of Canada in *R v. Mohan*: (1) relevance; (2) necessity in assisting the trier of fact; (3) the absence of any exclusionary rule; and (4) a properly qualified expert.⁶³ The evidence will not be admitted if the court finds that the expert opinion does not meet this criteria.

Once expert evidence is admitted, the trier of fact (typically a judge, as opposed to a jury, in commercial matters) determines how much weight is to be afforded to an expert's testimony when reaching its conclusion.⁶⁴ For example, in *Rousta v. MacKay*, even though the court admitted the expert's opinion into evidence, it placed no weight on the opinion concerning the valuation of the plaintiff's future income-earning capacity.⁶⁵ This was because the expert's methodology and assumptions had failed to account for certain factors when projecting for the plaintiff's businesses future income. In this case, the expert had made a projection assuming the plaintiff would work full-time, without considering that throughout the business' past performance the plaintiff had only worked part-time.⁶⁶

iv Independence of experts

In order to be considered a properly qualified expert under the *R v. Mohan* framework, the expert must be able to fulfil his or her overriding duty to give an opinion that is impartial, independent and absent of bias.⁶⁷ The impartiality and independence of an expert is a threshold requirement that the court considers in determining whether the expert is properly

60 For more information relating to the jurisdiction, see the Provincial Rules of Practice and Provincial and Federal Evidence Acts.

61 For further discussion on how Canadian courts weigh the evidence of parties, please see Cudmore, *supra* note 58 at Recommended Readings: Prem M. Lobo and Peter J. Henein, 'Credibility under scrutiny: A study of the weight placed on expert valuation and damages evidence in Canadian court judgments.'

62 *ibid.*

63 *R v. Mohan*, [1994] 2 S.C.R. 9 at pp. 20-25, 1994 CanLII 80 [*Mohan*].

64 Cudmore, note 59 at ch.14.1; *Mohan*, note 63 at paras. 149.

65 *Rousta v. MacKay*, 2018 BCCA 29 at para. 22-28 (CanLII).

66 *ibid.*

67 *White Burgess Langille Inman v. Abbott and Haliburton Co.*, 2015 SCC 23 at paras. 32, 46 (CanLII).

qualified to give an opinion on the issue in question prior to admitting his or her evidence.⁶⁸ Expert evidence should be ruled inadmissible if the expert is not impartial, in the sense that they cannot objectively assess the questions at hand.⁶⁹ Expert evidence is also inadmissible when it is established that he or she is providing evidence that is not the product of his or her independent judgement.⁷⁰

Many provinces and territories also provide explicit requirements related to the independence of expert witnesses.⁷¹

Independence does not require that counsel and the retained expert do not consult with one another in preparing for litigation. For example, in *Moore v. Getahun*, the Ontario Court of Appeal determined that consultation and collaboration between counsel and expert witnesses is essential to ensure that the expert's report assists the court in determining the issues. Collaboration between counsel and a retained expert does not necessarily erode the ability of the expert to remain independent and objective.⁷²

A recent example that illustrates the importance of an independent expert is *Davies v. The Corporation of the Municipality of Clarington*.⁷³ In this case, a plaintiff who had been injured retained an accountant to give evidence regarding the plaintiff's past and future earning capacity.⁷⁴ Finding that the expert's evidence was 'little more than a regurgitation of what he was told' by the plaintiff, the Ontario Superior Court excluded the evidence because the expert had not independently reviewed the evidence in reaching their conclusions.⁷⁵ The exclusion of this evidence left the plaintiff without an expert to assist the court in quantifying his losses. Instead, the trial judge quantified damages after considering documentary and lay witness evidence. The trial judge made no award for past or future loss of income.⁷⁶ The plaintiff had requested damages in excess of US\$60 million, partly comprised by his request for US\$2,555,136 per annum to age 65 for past and future loss of income.⁷⁷ Instead, the plaintiff was awarded general damages of US\$50,000.

68 *ibid* at paras. 52-54.

69 *ibid* at para. 11.

70 *ibid*.

71 In Nova Scotia, for example, the Civil Procedure Rules require that an expert's report be signed by the expert who must make (among others) the following representations to the court: that the expert is providing an objective opinion for the assistance of the court; that the expert is prepared to apply independent judgement when assisting the court; and that the report includes everything the expert regards as relevant to the expressed opinion and draws attention to anything that could reasonably lead to a different conclusion (Section 55.04(1)(a), (b) and (c)). The Queen's Bench Rules (Saskatchewan), Section 5-37; Supreme Court Civil Rules, B.C. Reg. 168/2009, Section 11-2(1); Rules of Civil Procedure, R.R.O. 1990, Reg. 194, Section 4.1.01(1); Rules of Court, Y.O.I.C. 2009/65, Section 34(23). Moreover, the rules in Saskatchewan, British Columbia, Ontario, Nova Scotia, Prince Edward Island, Quebec and the Federal Courts require experts to certify that they are aware of and will comply with their duty to the court: Saskatchewan Queen's Bench Rules, Section 5-37(3); British Columbia Supreme Court Civil Rules, Section 11-2(2); Ontario Rules of Civil Procedure, Section 53.03(2.1); Nova Scotia Civil Procedure Rules, Section 55.04(1)(a); Prince Edward Island Rules of Civil Procedure, r. 53.03(3)(g).

72 *Mohan*, note 63 at paras. 56, 63-66.

73 2018 ONSC 4370 (CanLII).

74 *ibid* at para. 79.

75 *ibid* at paras. 95-96, 113-114.

76 *ibid* at para. 451.

77 *ibid* at para. 6.

v Challenging expert's credentials

As discussed, an expert must be properly qualified to give evidence on the subject matter to which his or her testimony relates. An expert's credentials are considered by Canadian courts in qualifying the expert.⁷⁸ Once the trial judge rules that the witness has the requisite credentials to provide opinion evidence in relation to a damages assessment, the extent of the expert's accomplishments and experience is a matter of weight to be given to that expert's opinion.⁷⁹

At the admissibility or qualification stage, whether the expert has the requisite credentials or not depends on particular facts of the case, the expert and the opinion that he or she is offering.⁸⁰ Canadian courts do not apply a rigid analysis in assessing an expert's credentials. As long as the trial judge is satisfied that the witness is sufficiently experienced, the court will not focus on whether the expertise was derived from specific studies or by practical training, although that may affect the weight to be given to the evidence.⁸¹

On the issue of weight, the more tailored a party's expert's credentials are to the expert opinion he or she is providing, the more likely that the party's expert's opinion will be given accepted or favoured by the court.⁸² This is especially important if the court is faced with opposing experts who are similarly qualified. For example, in *Orr v. Metropolitan Toronto Condominium Corp. No. 1056*, both experts were qualified to give an opinion regarding the valuation of the difference between a two-storey and three-story condominium unit. However, the court preferred the evidence of the plaintiff's expert. This was in part because one of the defendant's experts had testified that they were not familiar with the authoritative textbook for appraisers in Canada.⁸³

78 Sopinka, Lederman & Bryant, *The Law of Evidence in Canada* (Toronto: LexisNexis 2018) at p. 854. [Sopinka].

79 *ibid.*

80 *R v. Pham*, 2013 ONSC 4903 at para 31. In the context of a drug case involving a large quantity of heroin, Durno J set out a lengthy list to consider in determining whether a proposed expert witness is adequately qualified. The factors listed are as follows: the manner in which the witness acquired the special skill and knowledge upon which the application is based; the witness' formal education (i.e., degrees or certificates); the witness' professional qualifications (i.e., a member of the College of Physicians and Surgeons); the witness' membership and participation in professional associations related to his or her proposed evidence; whether the witness has attended additional courses or seminars related to the areas of evidence in dispute; the witness' experience in the proposed area(s); whether the witness has taught or written in the proposed area(s); whether, after achieving a level of expertise, the witness has kept up with the literature in the field; whether the witness has previously been qualified to give evidence in the proposed area(s), including the number of times and whether the previous evidence was contested; whether the witness has not been qualified to give evidence in the proposed area(s) and if so, the reason(s) why; and whether previous case law or legal texts have identified the contested area as a proper area for expert evidence and, if so, who might give the evidence. After considering these factors, Durno J found that a police officer could testify (with the exception of a few issues) based on his years of experience dealing with heroin users, although he had no scientific background.

81 Sopinka, note 78 at p. 853 (emphasis added).

82 See for example: *Municipal Property Assessment Corp., Region No. 15 v. Clublink Corp.*, 2009 64 O.M.B.R. 225; CarswellOnt 8241. The defendant put forth an expert to opine on the valuation of golf course facilities. The expert had numerous professional certifications specifically regarding the appraisal of golf courses, and was considered a 'leading authority'.

83 *Orr v. Metropolitan Toronto Condominium Corp. No. 1056*, 2016 ONSC 7630 at paras. 28, 33, 2016 CarswellOnt 19819.

vi Novel science and methods

An expert opinion that is based on novel science or a novel methodology must meet the same framework for admissibility as set out above. The Supreme Court of Canada has further held that a novel scientific theory or technique is subject to special scrutiny. Prior to being admitted, an opinion based on novel science must satisfy the basic threshold test of reliability.⁸⁴ While there is a more intense investigation into the reliability and validity of the science underlying the opinion, there is no requirement that the science on which the opinion is based must be generally accepted in the scientific community.⁸⁵

A court may evaluate the reliability of novel science or methods based on factors identified by the US Supreme Court in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, which has been adopted in Canada.⁸⁶ These factors include whether the theory or technique can be and has been tested; whether the theory or technique has been subjected to peer review and publication; the known or potential rate of error or the existence of standards; and whether the theory or technique used has generally been accepted.⁸⁷ This is a flexible analysis and these factors are non-exclusive.⁸⁸ What factors the court considers and the weight given to each is case specific.⁸⁹

vii Oral and written submissions

In Canadian litigation, both parties in a trial before a judge may make both oral submissions and written submissions regarding what the appropriate damages award would be if liability is established. In trials before a jury, there are typically only oral submissions to the jury.

IV RECENT CASE LAW***Borrelli v. Chan***

In 2018, the Ontario Superior Court of Justice awarded US\$2.6 billion in damages to SFC Litigation Trust after finding that Allen Chan (Chan), the former CEO of Sino-Forest Corporation (Sino-Forest), committed fraud and breached his fiduciary duty owed to Sino-Forest.⁹⁰ This decision is the largest judgment of its kind in Canadian history, and is notable in a number of respects. Justice Penny's decision also highlights the general principles that the Canadian law of damages rests upon.

The decision is currently under appeal, the outcome of which may have considerable implications for Canadian damages law. In particular, the outcome will inform damages awards arising from cross-border litigation in Canada and the United States, as well as damages associated with claims of fraud and the breach of fiduciary duties owed to a large, publicly traded corporations.

84 *Mohan*, note 63 at para. 28.

85 *R. v. J.-L.J.*, [2000] 2 S.C.R. 600 at para. 34, 2000 SCC 51 (CanLII).

86 *ibid* at para. 33.

87 *ibid*.

88 *R v. Trochym*, 2007 SCC 6 at para. 139 (CanLII).

89 *ibid* at para. 139-141.

90 *Borrelli*, note 10 at para 1.

The facts of the case

Sino-Forest was a publicly traded company listed on the Toronto Stock Exchange. It was a successful forest plantation operator with assets primarily in China.⁹¹ It suffered catastrophic losses in 2011 following the publication of a negative analyst's report by Muddy Waters. The Muddy Waters Report accused Sino-Forest of effectively operating as a Ponzi scheme, and being rife with fraud, theft and undisclosed related-party transactions.⁹²

An independent committee of Sino-Forest's board of directors determined that the allegations were largely correct, and that Chan and other members of the senior management team were involved in the control of counterparties that had engaged in transactions with Sino-Forest. The Ontario Securities Commission commenced proceedings against both Sino-Forest and Chan. As a result of these allegations, Sino-Forest collapsed and filed for protection under the Canadian Companies' Creditors Arrangement Act.

By virtue of a plan of compromise approved by the Ontario Superior Court of Justice, Sino-Forest's debtholders acquired the tangible assets of the company, which they later sold at a loss. Much of Sino-Forest's property and value was 'missing' and unaccounted for.⁹³ Sino-Forest's rights of action were assigned to the SFC Litigation Trust. Cosimo Borrelli was appointed by the debtholders as litigation trustee.⁹⁴ Mr Borrelli pursued Chan for US\$2.6 million in damages for the wrongs done and breaches of duty owed by Chan to Sino-Forest. These breaches had caused Sino-Forest to be unable to account for its missing funds and, ultimately, its failure.⁹⁵

The decision

Justice Penny found that Chan, in his position as CEO of Sino-Forest, had ultimately controlled all of Sino-Forest's operations, including the approval of all of Sino-Forest's wood log trading contracts.⁹⁶ Chan had also secretly controlled many of Sino-Forest's counterparties in a complex network of relationships with third parties. These third parties had acted as Chan's 'nominees', holding positions as directors, officers and shareholders on his behalf, to create the illusion that the transactions were on an arms'-length basis.⁹⁷ These relationships were never disclosed to Sino-Forest, although Chan had caused Sino-Forest to fund payments to these entities that were never recovered.

Justice Penny found Chan responsible for Sino-Forest's losses by finding that it was his fraudulent actions and corresponding breaches of his fiduciary duty as an officer of Sino-Forest that caused Sino-Forest to fail.⁹⁸

91 *ibid* at para. 9.

92 *ibid* at para. 2.

93 *ibid* at para 1022.

94 *ibid* at paras. 5, 72.

95 *ibid* at para. 127.

96 *ibid* at para. 12.

97 *ibid* at para. 342.

98 *ibid* at paras. 937-939.

The damages were calculated as US\$2,627,512,000. The losses were calculated as the net cash proceeds that Sino-Forest would have had to invest in legitimate business operations, plus punitive damages in the amount of US\$5 million.⁹⁹ The damages were awarded in US dollars, being the currency in which Sino-Forest reported its financial results.¹⁰⁰

The application of equitable principles to a compensatory damages award for loss arising from the tort of fraud and breach of fiduciary duty

The determination of the quantum of damages was a complex matter given the large and complicated fraud network that Chan had established. Justice Penny acknowledged that often, damages cannot be precisely calculated, but that the difficulty of assessing the damages was no ground to refuse substantial damages even if it amounted to 'guess work'.¹⁰¹ The parties had called experts to assist in quantifying damages. The experts diverged significantly in their methodologies for quantifying damages that arose from numerous fraudulent transactions.¹⁰² Justice Penny noted that the calculation of damages was 'ultimately a task for the court' and not for accountants or other mathematical and statistical experts.¹⁰³

In awarding damages for fraud, Justice Penny applied the basic principle that the damages for the tort of fraud were to be measured based on Sino-Forest's financial position 'but for' Chan's fraud.¹⁰⁴

A breach of the fiduciary duty entitles the wronged party to equitable compensation, and this damages assessment differs from the analysis that is applied to breaches of torts and contracts. Equity results in a presumption that is beneficial to the plaintiff:

Equity is concerned with restoration of the actual value of the thing lost through the breach of duty, in this case Sino-Forest's funds raised on the capital markets. Equitable compensation is assessed at the date of trial, not, like common-law damages, at the date of the breach. And, equity presumes the trust funds will be invested in the most profitable way or put to the most advantageous use.¹⁰⁵

Having found that equitable principles apply, Justice Penny rejected Chan's critique of the plaintiff's expert. The plaintiffs' expert had calculated the loss of the assets based on its value prior to the Muddy Waters Report, rather than when it was sold after its value had dropped.¹⁰⁶ Justice Penny found that Sino-Forest was not required to bear the risk of market fluctuation between the date of acquisition and date of sale, or prove that the transaction was not for fair market value.¹⁰⁷ Since Chan's fraud had created the negative impact on the assets' market value, the plaintiffs did not have to bear that loss and were entitled to compensation for the assets' value prior to the release of the Muddy Waters Report.

99 ibid at paras. 1026-1027, 1049.

100 ibid at para. 7.

101 ibid at para. 942.

102 ibid at para. 950.

103 ibid at para. 943.

104 ibid at para. 1022.

105 ibid at para. 1010 (emphasis added).

106 ibid at para. 1005.

107 ibid at para. 1011.

RUSSIA

*Yaroslav Klimov and Ekaterina Merkulova*¹

I OVERVIEW

In Russia, recovery of damages is a universal remedy available for a wronged party.

The universal nature means that, as a general rule, a wronged party may recover damages regardless of whether there are other remedies available to the party or whether the party's right to recover damages is specifically mentioned in law or in an applicable agreement.

Historically, claims for recovery of damages before the Russian courts have been very difficult to prove due to the high threshold of evidence required. For many years, the courts acted on the basis that both the amount of damages and causal link between the breach and the harm must be proved with 'absolute certainty'.

The trend for lowering the high evidential burden for recovery of damages began with the Supreme Arbitrazh (Commercial) Court of the Russian Federation² (the Supreme Arbitrazh Court) in 2011 when the court applied a lower standard of evidence in order to secure the interests of the party who suffered loss and render a fair judgment.

Substantial amendments to the Civil Code of the Russian Federation (the Civil Code) in effect from 1 June 2015 and additional clarifications of the provisions in the Civil Code dealing with recovery of damages that have been recently issued by the Supreme Court of the Russian Federation (the Supreme Court) have continued this trend of lowering the evidential standard and simplifying the procedure for evidencing damages claims.

i Amount of damages and causal link between the breach and the damage

The most important changes were introduced in relation to the threshold of evidence required to prove the amount of damages and the causal link between the breach and the damage.

According to the amended Civil Code, the amount of damages must be proved to 'a reasonable degree of reliability'. This test is significantly lower than the previous standard of 'absolute certainty'.

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2 There are two branches of civil courts in Russia: state arbitrazh (commercial) courts, primarily dealing with commercial disputes between legal entities, corporate and bankruptcy disputes, and courts of general jurisdiction, primarily dealing with non-commercial disputes between individuals. The Supreme Arbitrazh (Commercial) Court was the highest court for state arbitrazh (commercial) courts in Russia until 6 August 2014. Since 6 August 2014 the Supreme Court of the Russian Federation is the highest court for both state arbitrazh (commercial) courts and courts of general jurisdiction.

Furthermore, if a claimant fails to prove the amount of damages to a 'reasonable degree of reliability', it does not constitute a ground for dismissal of the claim. The court must still determine the amount of damages by taking into account all the circumstances of the case, based on principles of fairness and proportionality of liability stemming from the breach.

In addition, in relation to lost profit, the Supreme Court in its recent clarifications ruled that the calculation of the amount of lost profit need not be precise and may be based on approximation. For example, the amount of loss of profit may be calculated using the actual profit of the creditor for a similar period prior to the breach committed by the debtor.

According to the new rules, the causal link between the damage suffered and the breach will be established if such damage is deemed a normal consequence of the breach committed by the defendant. This is a new principle for the courts. Previously, the court required that the causal link is also proved with 'absolute certainty'.

Though the above amendments were introduced in relation to contractual damages, they should also apply in the context of tortious liability.

ii 'Concrete' and 'abstract' methods for calculating damages

Recent amendments to the Civil Code further simplify the process for proving damages by introducing the 'concrete' and 'abstract' methods of calculating damages. These methods were introduced into the Civil Code with effect from 1 June 2015 as a universal method that may be used when calculating damages in relation to all types of contracts. Previously, the Civil Code provided for these methods only in relation to supply agreements and there was no unified approach in court practice as to whether such methods were applicable to the calculation of damages in other types of contracts.

The 'concrete method' of calculation applies where a claimant has mitigated a loss by entering into a replacement transaction to replace an original transaction that has been terminated due to non-performance or improper performance by a defendant. The calculation is based on the price difference between the original transaction and the replacement transaction.

The 'abstract method' applies if a claimant has not mitigated its loss by entering into a replacement transaction, but where an actual price for similar goods or services can be established. The difference between the price in the original agreement and the actual price is used to calculate the amount of abstract damages.

iii Damages resulting from bad faith negotiations

The recent amendments to the Civil Code further extend possibilities for the wronged party to restore the rights violated during negotiations by introducing the notion of bad faith negotiations and requiring a party who negotiated in bad faith to compensate the other party for damages suffered. In particular, the party who negotiated in good faith will be compensated for expenses relating to the negotiations and the lost opportunity to enter into an agreement with a third party.

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

The Civil Code provides for two types of damages: (1) actual loss; and (2) lost profits.

Actual loss encompasses loss or damage to the property or assets of a party as well as subsequent costs the party has or will have to incur in order to restore that party to its original position.

Lost profits refers to income not obtained by the party, which would have been obtained under normal conditions, if there was no breach on the part of the defendant.

Unless otherwise provided by law or by contract, damages must be compensated in full. The intention is to place the party in the position that it would have been in if a breach had not occurred.

A claimant seeking to recover damages must prove: (1) that there is a breach on the part of the defendant; (2) the amount of harm suffered; and (3) a causal link between the breach and the harm suffered. As a general rule, the Civil Code also recognises that there must be fault on the part of the defendant. However, the fault is presumed and, therefore, the burden lies with the defendant to satisfy the court that they are not at fault.

Moreover, in instances provided by the Civil Code, a party that causes the damage is held liable regardless of whether such party is found to be at fault for the breach or not. For example, where damage arises from the breach of a commercial contract, the party may only be released from liability in case of force majeure.

ii Evidence

There is no specific type of evidence required in Russia to prove damage. Depending on the complexity of the circumstances of the dispute, the claimant may need to provide expert reports and additional types of evidence to prove the amount of damage. In complex disputes, the courts tend to rely on expert evidence.

iii Date of assessment

As a general rule, unless otherwise provided by law or by contract, there are two main approaches to assessing the date on which damages are calculated, along with a third, less commonly used approach.

Day of voluntary performance

The first approach applies when the party who caused damage voluntarily agrees to compensate the other party. Here damages are calculated based on the price of goods or services on the day of voluntary performance.

Day the claim was submitted

The second option applies when the court finds the defendant liable for damages suffered by the claimant. Here damages are calculated based on the price of goods and services on the day the claim was submitted to the court.

Date of the judgment

There is a third approach the court may apply at its own discretion. The court has discretion to calculate damages by taking into account the price of goods and services on the date of the judgment. This discretion allow the court the flexibility to render a fair judgment in cases where, for example, prices have fluctuated significantly by the date of judgment.

iv Financial projections

Russian law does not directly mention financial projections in relation to the calculation of damages. However, the Civil Code does allow a claimant to factor into its damages calculation (1) the costs that it projects it will be forced to incur in order to recover from the breach (the non-concrete part of real damage), and (2) any profits not made (as lost profit). Therefore, the Civil Code allows a consideration of financial projections to some extent when calculating damages.

Following amendments to the Civil Code (which came into effect from 1 June 2015) and further clarifications of the Civil Code by the Supreme Court, the threshold required to prove the amount of damages has reduced from 'absolute certainty' to 'a reasonable degree of reliability'. This in turn has increased the scope for using financial projections in the calculation of damages.

However, despite the reduced threshold required to prove the amount of damages and the increased scope for the use of financial projections, the courts have tended towards more conservative approaches when calculating damages. Where the circumstances would allow for use of financial projections, the court have favoured approaches that have less reliance on expert speculations. For example, in one recent case where the claim was for recovery of lost profit, the court adopted an approach that had a stronger correlation with the factual evidence, leaving smaller scope for interpretation by an expert.

v Assumptions

A claimant seeking to recover damages may rely on the following presumptions.

Fault

As a general rule, the fault of the defendant is presumed, unless proved otherwise. The burden lies with the defendant to satisfy the court that they are not at fault.

Amount of damages

In order to prove the amount of damages suffered, the claimant is required to present evidence sufficient for the court to determine the amount of damages to the standard of 'a reasonable degree of reliability'.

Amount of lost profit

Where the defendant has profited from a breach, there is a presumption that the claimant can recover at least the amount of the defendant's profit that flows from the breach.

Causal link

The causal link between the damage suffered by the claimant and the breach is presumed to be proved if the damage suffered is a normal consequence of the breach.

In addition, there are certain presumptions applicable to specific situations.

- a* Abstract and concrete damages: when calculating concrete damages (explained in the overview above), it is presumed that a claimant entered into the replacement transaction in good faith and reasonably.
- b* Bad faith negotiations: as a general rule, it is presumed that negotiating parties act in good faith. By itself the refusal to continue negotiations without specifying reasons does not mean that a party is acting in bad faith.

However, in the following situations, the above presumption is reversed and a party is presumed to have entered into negotiations in bad faith:

- a* if a party provides the other party with incomplete or misleading information, including non-disclosure of material conditions that, taking into account the nature of the transaction, should be communicated to the other party; or
- b* if a party abruptly and unreasonably terminates negotiations where the other party could not reasonably expect such termination.

The defendant has the right to challenge any of the above assumptions.

vi Discount rates

Russian law does not take into account discount rates. A defendant does not have the right to apply to the court to request the awarded amount of damages be discounted based on the claimant's opportunity to invest the awarded amount.

vii Currency conversion

As a general rule, all payments in Russia must be made in roubles.

Regardless of whether the amount agreed by the parties is in a foreign currency or non-conventional monetary units (ECU, 'special drawing rights', etc.) payment is still required by law to be made in roubles.

By law the payment amount in roubles is determined according to the official exchange rate as of the day of payment. However, a different exchange rate or an exchange rate from a different date can be used where agreed by the parties.

Payments can be made in a foreign currency where permitted by the Federal Law on Currency Regulation and Currency Control No. 173-FZ dated 10 December 2003.

viii Interest on damages

As a general rule, if there is a delay in payment of damages required by a judgment or agreement, the creditor is entitled to require payment of interest on the outstanding amounts. Such interest is defined in the Civil Code as interest for 'unlawful usage of another person's money'.

Unless another interest rate is agreed by the parties or is provided for by law, the amount of interest due is calculated based on the key rate (or base rate) of the Bank of Russia, existing during the delay period. For example, from 17 September 2018, the key rate of the Bank of Russia is fixed at 7.5 per cent per annum.³

³ The Bank of Russia's Press Service information letter dated 14 September 2018.

If the interest rate agreed by the parties is higher than the key rate established by the Bank of Russia, the defendant can make an application to the court, which has discretion to reduce the amount of interest set by the parties if the court considers that the amount of interest is clearly inadequate considering the consequences of the breach, but not lower than the key rate of the Bank of Russia.

If damages are deemed recoverable by the court, interest on the damages will accrue from the date the judgment becomes effective.

If a party that caused damage and a party that suffered damage entered into a subsequent agreement pertaining to compensation for the damages, then interest will accrue in accordance with the terms of that agreement.

As a general rule, the interest will accrue until full payment of the amount due to the creditor is made.

If the delay in payment causes damage to the creditor and the amount of such damage is not fully covered by the amount of interest accrued for the delay period, then the creditor has the right to require the defendant to pay damages in excess of the amount of interest.

ix Costs

As a general rule, the unsuccessful party in a dispute must pay the successful party's costs. If the claim is only partially successful, costs will be allocated proportionately.

The successful party has the right to recover any costs deriving from the dispute – for example, any state fees relating to the dispute, amounts paid to the party's representatives, experts, specialists, witnesses, translators and others. The successful party may also recover costs incurred in relation to the collection of evidence, legalisation of documents received in another country, and issuance of a power of attorney. The list of costs that may be recovered by the successful party is not exhaustive.

Following the court's judgment on the merits of the case, the court will consider which party is liable for costs and to what extent, and the reasonableness of such costs. Costs are considered reasonable if they correspond to normal pricing.

The party required to pay costs can apply to the court to reduce the amount of costs, if the costs are proven to be unreasonable. For example, it is common practice in Russia for the court to significantly reduce the recoverable amount of fees paid to representatives. As a result, fees recovered may be several times lower than fees paid.

Though contingency fees are not prohibited by law, according to current court practice contingency fees are not recoverable.

x Tax

Payment of taxes is regulated by the Tax Code of the Russian Federation (the Tax Code).

Pursuant to the provisions of the Tax Code, damages received by a claimant (on the basis of a court decision or as a result of voluntary payment by the defendant), penalties and other sanctions are subject to 20 per cent corporate income tax in Russia, unless there is a double tax treaty between Russia and the country of residency of the creditor, which provides for a lower tax rate on received income.

It is important to note that the taxable amount of damages received by the claimant could be reduced based on what the claimant states as their expenses pursuant to the Tax Code.

The amount of damages, penalties and other sanctions received by the claimant are not subject to VAT. For many years there was no unified approach as to whether VAT may

be included by the claimant in the amounts of damages due to them. In 2013, the Supreme Arbitrazh Court ruled that VAT should not be included in the amount of damages due to the claimant, provided that the claimant has the right to VAT deduction. Generally, the courts follow this position.

III EXPERT EVIDENCE

i Introduction

Procedural rules for involving experts are established by the Civil Procedural Code of the Russian Federation⁴ (CPC) and by the Arbitrazh Procedural Code⁵ (APC).

The court has the right to involve an expert where it considers that specific professional knowledge is needed to resolve a dispute. This includes experts who are employees of state-owned or private expert organisations, or who have their own private practice.

There are no legal restrictions as to the qualifications of persons who may act as experts in court. The only exception is experts who are employees of state-owned organisations. According to the Federal Law on State Court and Expert Activities No. 75-FZ dated 31 May 2011 (the Law on State Court and Expert Activities), they must possess a higher education degree, additional professional education in a specific and relevant expertise area, and be qualified to conduct independent court examination. The level of expertise of state experts must be reconfirmed every five years.

The court also has the right to involve a 'specialist' to assist in resolving the dispute. The difference between a specialist and an expert is that the expert is involved by the court to conduct research and prepare an expert report reflecting their findings, while the specialist gives advice in a court hearing without conducting an examination and preparing a report. Specialists are rarely involved by Russian courts.

Also, in Russia it is common practice for a party to a dispute to hire its own expert, whom it believes is best qualified to conduct the examination. A party to the dispute will then formalise questions, and provide materials and documents to allow the expert to carry out the requested examination. Once ready, the party's expert report is submitted to the court. Though such reports cannot be considered expert reports as referred to in the APC and CPC, courts accept such reports and treat them as equal to other evidence.

ii The role of expert evidence in the calculation of damages

When calculating damages, Russian procedural rules do not give any preference to expert evidence over other sources of evidence available in a particular dispute.

When making a decision, the court will evaluate relevance, admissibility and reliability of each set of evidence separately and collectively.

This means that when rendering its judgment, the court may rely on the expert evidence as long as such evidence is not contradicted by other evidence presented to the court.

In practice, however, it is more common that contradictions arise between expert evidence provided by court-appointed experts and expert evidence presented by the parties.

4 The Civil Procedural Code of the Russian Federation establishes procedural rules for courts of general jurisdiction.

5 The Arbitrazh Code of the Russian Federation establishes procedural rules for state arbitrazh courts.

Based on analysis of available court practice and our own experience, in such instances, judges tend to prefer the opinions of court-appointed experts to the reports of party-appointed experts.

However, the Supreme Court has repeatedly stated that expert reports presented by the parties cannot be rejected simply on the basis that the experts who prepared such reports were not appointed by the court. In a recent case where the lower courts (i.e., first instance, appeal and cassation) accepted the findings of the court's expert report and rejected the expert report obtained by a party to the dispute, the Supreme Court, referring to the unresolved contradictions between the report of the expert retained by the claimant and the report of the expert appointed by the court sent the case for reconsideration to the first instance court. The Supreme Court ruled that contradictions between the court-appointed expert and the party's expert must be resolved when rendering the judgment.

iii The court's role excluding and managing expert evidence

In Russia, the court itself appoints the experts.

As a general rule, the court appoints the expert examination upon a motion of either party to the dispute. The court will consider that motion and if the motion is convincing then the court will initiate an expert examination. In the arbitrazh courts, the court may also proceed without an initial motion from either party and suggest the appointment of an expert. If either of the parties agrees, the expert examination will be appointed by the court.

The parties to the dispute have the right to present to the court their own expert candidates. The court is free to select experts from a proposed pool of candidates or to select its own candidates. In practice, the court generally selects experts from the candidates proposed by the parties.

The court will provide questions for the experts. The parties have a right to ask the court to add questions.

A request for expert examination must be filed with the court of first instance (i.e., the trial court). An expert examination may only be ordered by the court of appeal (the second level court) in a limited number of instances, for example, if the lower court refused to grant the party's motion to carry out the expert examination. Courts of higher instances (cassation courts and the supervisory court) cannot order an expert examination.

Parties have no right to challenge a court's rejection of a request for expert examination or the court's ruling on the appointment of an expert to conduct an examination (e.g., due to the court's choice of experts or questions for the experts). The only avenue to challenge these rulings is to appeal the court's judgment rendered on the merits of the case before the higher courts.

iv Independence of experts

Russian procedural rules require experts to act independently when conducting the expert examination initiated by the courts.

The following rights and obligations guarantee the independence of experts in court.

Disqualification and self-disqualification of experts

The CPC and the APC provide the grounds for disqualification of experts, which are similar to the standards for the judiciary.

The expert will be subject to disqualification if: (1) he or she is a relative of a party involved in the dispute or of a representative of such party; (2) he or she is personally, directly

or indirectly, interested in the outcome of the dispute, or there are other grounds that could raise doubts about his or her impartiality; (3) he or she is, or was, under employment or another position of subordination to a party involved in the dispute, or the representative of such party. This is not an exhaustive list.

The court may disqualify the expert on its own initiative. The parties to the dispute also have a right to request the disqualification of an expert. If there are grounds for disqualification, the expert can also self-disqualify.

Disqualification or self-disqualification must be done prior to commencement of consideration of the dispute on merits. After that, the disqualification or self-disqualification can only be requested if the grounds for disqualification became known to the requesting party after consideration of the dispute on merits commenced.

Expert fees

Experts receive their fees from the court upon completion of their examination. Prior to initiation of the examination at the request of the court, the parties to the dispute are required to transfer to the court's bank account the amounts due to the experts.

Provision of experts with materials for analysis

Experts are not allowed to contact the parties to the dispute directly. Materials necessary for the experts to conduct the examination are provided to them by the court. Experts can receive explanations from parties in a court hearing with a court's consent.

Expert independence in choosing the analysis method

The expert has the right to choose a method of analysis that provides validity, credibility and can be verified by using generally accepted scientific and practical data.

Criminal liability of the expert for giving a knowingly false opinion

An expert is criminally liable for knowingly giving a false opinion.

Criminal liability for influence on the expert or his or her relatives

Both the court and the parties to the dispute are prohibited from influencing the conclusions of the expert examination. Any party deemed to have influenced the expert will be subject to criminal liability under the Russian Criminal Code of the Russian Federation.

v Challenging expert credentials

Prior to initiation of the expert examination

Expert candidates proposed by the parties will be considered at a court hearing.

The parties have a right to present arguments as to why the expert candidates proposed by the opposing party should not carry out the required expert examination. In practice, the most common argument is the absence of the necessary education and experience in relation to the matter.

After completion of the expert examination

Questioning of expert

Any of the parties to a dispute can request that an appointed expert appears before the court for questioning. However, it is ultimately at the discretion of the court whether it considers that questioning is necessary in order to clarify aspects of a written expert report. The court is, therefore, entitled to refuse such a request.

Additional and repeated expert examination

If an expert report lacks certain necessary findings, either party to the dispute or the court may request that the court appoint another expert examination. In such circumstances a party may request an additional expert examination into the outstanding issues by the same or a new expert, or make a request to have the expert examination repeated in its entirety by a new expert.

After consideration of the dispute on merits

After the first instance court has handed down its judgment on the merits of the claim, the parties will also have an opportunity to raise disagreements with the expert opinion when challenging the first instance judgment in the higher courts (i.e., court of appeal, cassation or supervisory court).

vi Novel methods and science

The Civil Code establishes only a general framework for damages calculation. In particular, the Civil Code: (1) defines that damages should be calculated with a ‘reasonable degree of reliability’; (2) establishes that the calculation of loss of profit may be based on approximation; and (3) allows experts calculating the amount of damages the right to use methods of calculation of concrete and abstract damages (as explained in more detail above).

Furthermore, the Law on State Court and Expert Activities contains the general rule that an expert must carry out his or her examination objectively, thoroughly and fully, based on scientific and practical standards within the limits of his or her specialisation. The expert’s opinion must be based on assumptions that are verifiable and relevant, and must draw reliable conclusions derived from the scientific and practical data.

In addition, there are subordinate legislative acts that define the methodology for calculating damages in specific cases. For example, there is a specific methodology for the calculation of damages arising from the illegal dissemination of insider information.⁶

vii Oral and written submissions

Experts are required to issue their reports in writing.

IV RECENT CASE LAW

In a recent case, the claimant succeeded in obtaining judgment for the largest amount of damages successfully claimed to date in Russia. In this case, the new majority shareholder

⁶ Adopted by the Decree of the Federal Financial Markets Service of the Russian Federation dated 28 June 2012 No. 12-49/pz-n.

of a company and the company itself submitted a claim to a Russian state arbitrazh court to require former shareholders of the company to compensate the company for damages of 170 billion roubles. The new majority shareholders claimed that damages were suffered by the company as a result of a reorganisation undertaken by the former majority shareholders between the end of 2013 and the beginning of 2014.

In August 2017, the court awarded damages in the claimants' favour for 136 billion roubles. The court of appeal rejected the defendants' appeals and upheld the lower court judgment. The defendants chose not to appeal the judgment further, and the parties agreed a settlement.

According to the settlement agreement approved by the court in December 2017, the defendants agreed to pay to the claimants 100 billion Russian roubles to compensate for damages.

In another recent case, a buyer under a power supply agreement (the original agreement) submitted a claim to a Russian state arbitrazh court to recover from a seller under the original agreement concrete damages calculated as the difference between the prices for power supply in the original agreement and the replacement agreement (i.e., the agreement entered into between the buyer and the other power supply company).

The court held that the seller was liable for damages suffered by the buyer. The court found that the seller repeatedly breached the original agreement, therefore enabling the buyer to unilaterally terminate the original agreement and enter into a replacement agreement. As the price for power supply in the replacement agreement was higher than in the original agreement, the buyer was lawfully entitled to the difference in prices to be compensated as damages. The higher courts, including the Supreme Court in August 2018, subsequently upheld the judgment.

In another recent case, the Russian state arbitrazh court ruled that a defendant had acted in bad faith when it terminated negotiations that had been ongoing for more than six months. The defendant terminated the negotiations after it received from the claimant a signed lease agreement that had been agreed in its final form. As the claimant had to terminate lease agreements with former lessees in order to prepare a warehouse for the defendant, the court found in favour of the claimant and calculated lost profits based on lease payments the claimant would have received from its former lessees. The court ruled that the defendant had acted in bad faith as it had abruptly and unreasonably terminated negotiations in circumstances where the claimant could not reasonably expect such termination. The higher courts, including the Supreme Court in May 2018, upheld this judgment.

In another case, the claimant (a power generation company) claimed lost profits of approximately 1.3 billion roubles from the defendant (a company that supplied, assembled and set into operation power-generating equipment). The court, pursuant to the (newly established) rule that there is a presumed causal link if damage is a usual consequence of the breach, agreed that the claimant's inability to sell power on the wholesale electricity power market occurred as a consequence of equipment supplied by the defendant, which was of insufficient quality. The court ruled that the claimant could recover from the defendant damages calculated as income the claimant would have received if the equipment had been of proper quality.

The higher courts agreed with the judgment of the first instance court; however, recalculated the amount of damages and reduced the damages to approximately 820 million roubles in October 2017.

SINGAPORE

*William Ong*¹

I OVERVIEW

The approach of the Singapore courts with regard to compensatory damages claimed in civil litigation has been based on the usual principles like causation, remoteness of damages, and mitigation. The claimant or plaintiff bears the burden of proving both the fact and amount of loss, and therefore must adduce sufficient evidence to quantify the damage.² In terms of proving loss suffered by the plaintiff in claims for unliquidated damages, the Court of Appeal in Singapore has stated that an award of compensatory damages in contract law should be based ideally on the plaintiff's own loss rather than measuring it by reference to the defendant's gains or profits.³

Most notably perhaps, the Singapore courts have remained committed to the traditional principles of remoteness of damages espoused under *Hadley v. Baxendale*,⁴ declining to follow the new test set out by Lord Hoffman in *The Achilles*,⁵ which is whether the defendant assumed responsibility for the loss that arose from the breach. Thus in *MFM Restaurants Pte Ltd v. Fish & Co Restaurants Pte Ltd*, the Court of Appeal expressly decided against adopting the 'assumption of responsibility' test, pointing out, *inter alia*, that the 'assumption of responsibility' approach (which is agreement-centred and based on whether the contract breaker had, on a true interpretation of the contract, assumed responsibility) appeared to exclude the operation of the very doctrine of remoteness of damage in contract law itself.⁶ The Court of Appeal was concerned with the practical uncertainties in applying this new test, given that parties at the time of entering the contract would usually not be thinking of assuming responsibility for the consequences of a future breach.⁷ The Court thus rejected Lord Hoffman's approach, except to the extent that the concept of assumption of responsibility is already incorporated in both limbs of *Hadley v. Baxendale*.⁸ The position under Singapore law was reaffirmed in *Out of the Box*,⁹ where the Court of Appeal reiterated its preference

1 William Ong is a partner at Allen & Gledhill. The author would like to thank Dion Loy, trainee at Allen & Gledhill LLP, for his assistance in the production of this chapter.

2 *Robertson Quay Investment Pte Ltd v. Steen Consultants Pte Ltd and another* [2008] 2 SLR(R) 623; [2008] SGCA 8 at [27].

3 *MFM Restaurants Pte Ltd and another v. Fish & Co Restaurants Pte Ltd and another appeal* [2011] 1 SLR 150 at [66].

4 (1854) 9 Exch 341; (1854) 156 ER 145.

5 [2009] 1 AC 61; [2008] UKHL 48.

6 *MFM Restaurants* (No. 3) at [92]–[95].

7 *ibid* at [92]–[100].

8 *ibid* at [140].

9 *Out of the Box Pte Ltd v. Wanin Industries Pte Ltd* [2013] 2 SLR 363; [2013] SGCA 15.

for the orthodox approach under *Hadley*. The Court also stressed that, conceptually, ‘it is important that cases that in fact concern the interpretation of a contract in order to identify the specific nature of the obligation that has been undertaken not be conflated, or for that matter confused, with cases that truly are concerned with questions of remoteness.’¹⁰

While this is a section on compensatory damages, it should be noted that the Singapore courts have expressed caution on the award of restitutionary damages recognised by the UK courts under *AG v. Blake*,¹¹ or at least the characterisation of *AG v. Blake* damages as restitutionary in nature. *AG v. Blake* was an exceptional case, where the defendant breached his contractual undertaking not to divulge official information gained as a member of the UK intelligence service by entering into a publishing deal for his autobiography, and where the Attorney General sought a full account of his wrongfully gained profits. *AG v. Blake* therefore allowed the award of damages based on the defendant’s gains or profits, rather than the plaintiff’s losses. The Court of Appeal in Singapore held that the main difficulty with recognising *AG v. Blake* damages as a part of Singapore law is the uncertainty of the legal criteria to be applied in awarding such damages.¹² Nonetheless, the Court left open the possibility that *AG v. Blake* damages could be recognised, although the precise status and scope of this category of damages under Singapore law is likely to remain unresolved until it is determined by the Court in the future.¹³

In addition, while the Court of Appeal recently accepted *Wrotham Park* damages as a part of the contractual remedies available under Singapore law, its approach differs from the UK position in some important respects that will be briefly discussed below.¹⁴

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

The quantification of financial loss usually underpins any compensatory claim for damages – while such quantification may involve technical evidence assisted by the relevant experts, it is usually on the basis that damages should compensate the plaintiff for the defendant’s wrongdoing. In tort, the purpose of damages is to put the claimant back into the position in which he would have been, if the tort had not been committed.¹⁵ In a contractual claim, damages seek to put the plaintiff in the position he or she would have been in had the contract been performed; this is often seen as compensation for the plaintiff’s expectation loss – such expectation loss would encompass the plaintiff’s total (or gross) loss – including the expected (or net) profit that the plaintiff would have received had there been no breach of contract as well as his or her expected expenses, which he or she would have recouped if the contract had been performed.¹⁶ Both approaches in tort and contract are compensatory, and seek to compensate the claimant for his or her loss. Hence, quantification of financial loss in contractual claims would often be premised on a valuation of the position which the plaintiff

10 *ibid* at [29].

11 *Attorney-General v. Blake (Jonathan Cape Ltd Third Party)* [2001] AC 268.

12 *Turf Club Auto Emporium Pte Ltd and others v. Yeo Boong Hua and others and another appeal* [2018] SGCA 44 at [252]–[254].

13 *ibid* at [255].

14 See the ‘Recent Case Law’ section for a more thorough discussion.

15 *Swiss Butchery Pte Ltd v. Huber Ernst and others and another suit* [2013] 4 SLR 381 at [14].

16 *Turf Club* (No. 12) at [125].

would be in had the contract been performed, complete with the expected costs or expenses incurred in performing the contract. Quantification of financial loss for tort would involve an exercise of what would have happened if the tort had not been committed – so a conspiracy to divert business away from a claimant would involve assessing the revenue or profits which had been lost, complete with the expected costs or expenses in serving the customers had they not been diverted away by the conspirators.

An award of substantial damages where loss is asserted will only be justified where the court is satisfied as to both the fact of damage (i.e., the adverse consequence) and the amount.¹⁷ If the plaintiff satisfies the court on neither, he will at the most be awarded nominal damages where a right has been infringed or where liability is established.¹⁸

ii Evidence

It is well established that a plaintiff claiming damages must adduce before the court sufficient evidence of his or her loss. This approach has been affirmed by the Court of Appeal, which has held that proof of damage is very much a primary matter – topics such as remoteness and mitigation are potentially relevant only after there is proof of damage to begin with.¹⁹ Such proof depends wholly on the factual matrix concerned, which can take a myriad of forms.²⁰

That being said, where it is clear that some substantial loss has been suffered, the fact that an assessment is difficult because of the nature of the damage is no reason for awarding no damages or merely nominal damages.²¹ In this respect, '[w]here precise evidence is obtainable, the court naturally expects to have it, [but] where it is not, the court must do the best it can.'²² The Court must do the best it can on the evidence available and adopt a flexible approach where it is clear that some substantial loss has been incurred.²³

In doing its 'best', the courts will adopt a flexible approach,²⁴ so as to balance the plaintiff's burden of adducing sufficient evidence of his loss on the one hand, and the fact that absolute certainty and precision is impossible to achieve in some cases on the other.²⁵ In this regard, the Court of Appeal acknowledged the reality that 'some educated guesses have to be made – regardless of the precise methodology ultimately adopted by the court', and that 'life is far more complex than simple law school hypotheticals and even textbooks would have us believe.'²⁶

Thus, where the plaintiff has done its level best to prove its loss and the evidence is cogent, the court should allow it to recover the damages claimed.²⁷ Even where 'the available evidence on which to base an award of damages' is 'far from satisfactory', the courts are still able to award 'just and fair sums to plaintiffs if the legal rules and principles justified them.'²⁸

17 *Biofuel Industries Pte Ltd v. V8 Environmental Pte Ltd and another appeal* [2018] 2 SLR 199; [2018] SGCA 28 at [41].

18 Justice James Edelman, *McGregor on Damages* (20th edn, Sweet & Maxwell 2018) at para. 10-001.

19 *Robertson Quay* (No. 2) at [27].

20 *ibid.*

21 *McGregor on Damages* (No. 18) at para. 10-002.

22 *Biggin & Co Ltd v. Permanite, Ltd* [1951] 1 KB 422 at 438.

23 *Robertson Quay* (No. 2) at [30].

24 *ibid.*

25 *Ramesh s/o Krishnan v. AXA Life Insurance Singapore Pte Ltd* [2017] SGHC 197 at [65].

26 *MFM Restaurants* (No. 3) at [62].

27 *Robertson Quay* (No. 2) at [31].

28 *MFM Restaurants* (No. 3) at [62] and [65].

The flexible approach does not mean that a plaintiff could simply claim that evidence was not available or irrelevant without more. Where the plaintiff has failed to attempt its level best to prove its loss and adduce cogent evidence, this failure to meet the evidentiary threshold necessary to quantify its loss will result in the award of nominal damages only.²⁹

iii Date of assessment

As a general rule, damages for breach of contract or tort are assessed as at the date of breach.³⁰

In *The Golden Victory*,³¹ the UK Supreme Court held that this general rule is not inflexible, and that the courts are not precluded from taking into account events that occur subsequent to a breach of contract, if doing so would give effect to the overriding compensatory principle that the damages awarded should represent no more than the value of the contractual benefits of which the plaintiff had been deprived.

The High Court of Singapore has also recognised that the general rule that damages are to be assessed as at the date of the breach is not an absolute one. Thus the Court held that where it is necessary in order to compensate the plaintiff adequately for the damage suffered, or if it would otherwise lead to injustice, a different date of assessment can be selected.³²

In *Swiss Singapore Overseas Enterprises Pte Ltd v. Exim Rajathi India Pvt Ltd*,³³ the High Court distinguished *The Golden Victory* based on its facts – the overriding compensatory principle was that damages awarded should represent no more than the value of the contractual benefits which the claimant had been deprived and therefore where at the date of assessment an event had already happened that would have terminated the contract had it been still in place, the court should have regard to what actually occurred.³⁴ In *Swiss Singapore* there was a one-off sale and delivery contract, as opposed to the longer-term contract in *The Golden Victory* that provided for obligations to be performed over a period of time.³⁵

However, any notion that there is a material distinction between one-off contracts and contracts for performance over a prolonged period of time for the purposes of the date of assessing damages was rejected by the UK Supreme Court in *Bunge SA v. Nidera BV*.³⁶ In *Bunge v. Nidera*, there was a one-off contract for the sale and purchase of Russian milling wheat. Following Russia's introduction of an embargo on the export of wheat, the sellers notified the buyers of the embargo and purported to cancel the contract. The buyers treated this cancellation as premature, and thus a repudiation, which they accepted. On the assessment of damages, the sellers argued that, even if the termination was premature, the fact that shipment under the contract would have been subject to the ban when the time for shipment came meant that no loss had been suffered. The UK Supreme Court stated that the compensatory principle in *The Golden Victory* is not limited to instalment contracts, and awarded the buyers nominal damages. Lord Sumption held that '(t)here is no principled reason why, in order to determine the value of the contractual performance that has been lost

29 *Biofuel Industries* (No. 17) at [42]–[45].

30 *Tay Joo Sing v. Ku Yu Sang* [1994] 1 SLR(R) 765 at [36]–[37].

31 *Golden Strait Corpn v. Nippon Yusen Kubishika Kaisha* [2007] 2 AC 353 (HL).

32 *Justlogim Pte Ltd and another v. Oversea-Chinese Banking Corp Ltd and another* [2007] 1 SLR(R) 425; [2006] SGHC 209 at [66].

33 [2010] 1 SLR 573; [2009] SGHC 231.

34 *ibid* at [77].

35 *ibid* at [78].

36 [2015] UKSC 43.

by the repudiation, one should not consider what would have happened if the repudiation had not occurred', since this is 'fundamental to any assessment of damages designed to compensate the injured party for the consequences of the breach'.³⁷

While certainty as engendered by the breach date rule for assessment of damages may be valuable, the Courts have shown that they are willing to take into account supervening events which have occurred post-breach to ensure that the claimant is truly compensated for his loss). Although Swiss Singapore dealt with a one-off contract, the decision on which date to assess damages did not turn on whether the contract was a one-off contract or instalment contract. Thus the Singapore courts will, in accordance with the compensatory principle, exercise the flexibility of taking into account supervening events that have taken place by the date of assessment in order to ensure that the claimant is truly compensated for the loss he has suffered (if any).

iv Financial projections

Financial projections are sometimes necessary where a quantification of financial loss involves assessing loss of a prospective nature. For example, this may be achieved through a loss of profits analysis, whereby the plaintiff is awarded the difference between its actual profits and the profits it would have obtained 'but for' the defendant's breach. Alternatively, a business valuation analysis may be available, whereby loss is quantified as the diminution in value of a business, income stream or other specified asset as a result of the defendant's breach of contract.

The courts are cognisant of the fact that such financial projections, which involve projections into the future, are inevitably speculative to some degree.³⁸ As such, regardless of what calculation or valuation method is used for the financial projections, so long as the application of the method rests on certain assumptions, the court will look to scrutinise the reasonableness of these assumptions. In any event, the use of any projection or valuation method would be deemed inappropriate if it is significantly at variance with the evidence of what actually happened.³⁹

v Assumptions

It is common knowledge that each financial or valuation model for the purposes of loss assessment is highly dependent on its underlying assumptions. For instance, the discounted cash flow (DCF) model, which is widely used in both loss of profits and business valuation analyses, is nothing more than a calculation machine – the value that emerges from the model is completely dependent on the values it has been fed with.⁴⁰ The integrity of the financial model is thus dependent on the assumptions underpinning the specific method.

As such, where financial projections rest on certain assumptions, the court will consider both qualitatively whether the assumption is reasonable in light of the evidence and also quantitatively the likelihood of the assumed event actually materialising.⁴¹ For instance, if

37 *ibid* at [23].

38 *Poh Fu Tek and others v. Lee Shung Guan and others* [2018] 4 SLR 425; [2017] SGHC 212 at [41].

39 *Columbia Asia Healthcare Sdn Bhd v. Hong Hin Kit Edward and another and another appeal* [2015] 2 SLR 395 at [38]. (NB. This was in the context of a share valuation dispute.)

40 D Frykman and J Tolleryd, *Corporate Valuation – an easy guide to measuring value*, p. 88.

41 *Poh Fu Tek* (No. 38) at [42]; see also the Australian case of *Pownall v. Conlan Management Pty Ltd* (1995) 16 ACSR 227, where evidence pertaining to financial projection and valuation of shares was deemed

one were to make a projection based on the DCF model, that likelihood of the assumption materialising – to the extent that it is found to be less than a certainty – represents a risk to the business that must be accounted for in the analysis.⁴² As such, parties looking to rely on the various models for financial projections or valuations ought to be aware that such projections are not just a matter of arithmetical calculation – obtaining reliable information and making credible assumptions for the financial model are just as important in producing an accurate valuation or assessment.

vi Discount rates

It is generally accepted that a discount has to be given for accelerated receipt of any sums that had not fallen due at the date of the breach (i.e., future loss of profits), so as to properly account for the potential interest accrued by the plaintiff until the final date on which money would have been due. An award of compensation that failed to take this into account would overcompensate the plaintiff.⁴³ This is largely standard practice – the High Court has recognised that ‘this was the discount to be given to the [defendant] because the damages were being crystallised at one go and [the plaintiff] would be paid the damages immediately instead of having the payment stretched over a number of years’.⁴⁴

In addition, many financial projections, especially those involving cash-flow models, do factor in discount rates that are applied to the projected cash flows. For instance, under the DCF model, a discount rate is applied to transform the future cash flows into their net present value. This discount rate should reflect the risk inherent in the forecast future cash flows, and can, for example, be the company’s or business’ weighted average cost of capital (WACC),⁴⁵ which is a measure of a company’s return to those who finance its business by both debt and equity.⁴⁶

Where the court finds that the discount rate used in a particular financial projection fails to reflect certain risks to the business, it will not shy away from making an appropriate adjustment to account for those risks.⁴⁷ Thus, in *Poh Fu Tek*, the High Court increased the discount rate to reflect the risk of the company losing the right to continue its operations at its two key properties, and the risk that a major customer may not place any orders with the company in the future.⁴⁸

vii Currency conversion

The law on currency conversion for damages is governed by the *Miliangos* principle, which establishes that an English court could give judgment for a sum of money expressed in

inadmissible because the assumptions underlying the DCF valuation were not proved.

42 *ibid.*

43 *Christopher Moran Holdings Ltd. v. Bairstow and another* [2000] 2 AC 172 at 184E. Though this is in the context of a disclaimer of a lease by a liquidator, the court held that assessing compensation payable pursuant to a statutory right of compensation arising from the disclaimer is ‘precisely the same exercise as has to be undertaken when assessing the damages for a breach of contract’: see 180D.

44 *Swiss Butchery* (No. 15) at [22].

45 D Frykman and J Tolleryd (No. 40) pp. 72–78; see also Christopher Glover, *The Valuation of Unquoted Companies* (4th Edn, Thomson Gee 2004), pp. 240–244.

46 *Poh Fu Tek* (No. 38) at [110].

47 *ibid.*

48 *ibid* at [124]–[130].

foreign currency and, if it was necessary to execute on the judgment, the judgment in foreign currency would be converted to local currency on the date when the plaintiff was given leave to levy execution.⁴⁹

This principle has been applied in Singapore, and the High Court has confirmed that there is no right of election – of asking for judgment in local currency or for conversion of the judgment sum from foreign currency to local on a date other than the date of execution – open to the plaintiff.⁵⁰ The Court reasoned that the rationale for the *Miliangos* doctrine was that it was right to allow judgment to be entered in a foreign currency either because it was the relevant currency of the transaction or because it was the currency in which the plaintiff had most truly suffered his loss. In addition, the House of Lords in *Miliangos* was not giving the plaintiff an option to select his currency but was instead redefining the obligation of the debtor to pay the sum owed in the relevant currency, and had found that using the date on which the court authorised execution as the date for conversion of the foreign currency into the local currency was nearest to securing to the plaintiff exactly what he bargained for.⁵¹ This underlying rationale would thus be instructive as to when a Singapore court could give judgment for a sum of money expressed in foreign currency.

viii Interest on damages

The power of the Singapore courts to award interest on damages is derived from Paragraph 6 of the First Schedule of the Supreme Court of Judicature Act. Section 12 of the Civil Law Act allows the court to order that interest be awarded on the judgment sum at such rate as it thinks fit on the whole or any part of the debt or damages for the whole or any part of the period between the date when the cause of action arose and the date of the judgment.

A plain reading of Section 12 suggests that interest is not awarded as of right – it is a matter of the court’s discretion.⁵² However, as a matter of principle, plaintiffs who have been kept out of pocket without basis should be able to recover interest on money that is found to have been owed to them from the date of their entitlement until the date it is paid. Thus the purpose of the judicial discretion is to enable the courts to achieve justice according to the unique circumstances of each case. Such discretion would extend to a determination of whether to award interest at all; what the relevant rate of interest should be; what proportion of the sum should bear interest; and the period for which interest should be awarded.⁵³

The general rule is that interest should commence from the date of accrual of loss; however, this is subject to the court’s discretion to order that interest run from a date later than the date of accrual of loss. The court can therefore delay the start date for calculating interest where there has been an unjustifiable delay on the part of the plaintiff in bringing his action to trial.⁵⁴ Thus in *Robertson Quay*, the Court of Appeal ordered that interest on

49 *Miliangos v. George Frank Ltd* [1976] 1 AC 443.

50 *Indo Commercial Society (Pte) Ltd v. Ebrahim and another* [1992] 2 SLR(R) 667; [1992] SGHC 230.

51 *ibid* at [35].

52 *Grains and Industrial Products Trading Pte Ltd v. Bank of India and another* [2016] 3 SLR 1308; [2016] SGCA 32 at [138].

53 *ibid*.

54 *ibid* at [139].

damages awarded should run only from the date of service of the statement of claim. The Court departed from the general rule because of the plaintiff's unwarranted delay (of five years after its loss accrued) in commencing the suit.⁵⁵

With respect to the nature of the interest awarded, Section 12 of the Civil Law Act specifically enables the courts to award simple pre-judgment interests on debts and damages – the provision does not authorise the award of compound interest. However, the High Court has found that this did not necessarily prohibit the Court from granting compound interest *per se* or from granting damages assessed with reference to the actual compound interest lost or foregone by the plaintiff who had suffered those damages.⁵⁶ Thus the Court held that the Singapore courts have an 'unfettered discretion to award simple or compound interest as damages'. This approach 'accords with commercial and economic reality' and would better reflect a plaintiff's loss because if it were otherwise, a plaintiff in a long-running case risks being severely under-compensated in damages, especially where the interest rate was ascertained to be very high.⁵⁷

The key distinction here is between 'interest as damages' and 'interest upon the damages'. Section 12(2)(a) of the Civil Law Act states that nothing in the section 'shall authorise the giving of interest upon interest', but the Court has held that this section will not apply to an award of interest as damages, which comprises of the loss to the plaintiff assessed with reference for instance to the compound interest that the money could possibly have earned. This separate head of damage represented by the compound interest is therefore not within the scope of Section 12.⁵⁸

ix Tax

Any quantification of financial loss (and subsequent calculation of the quantum of damages) must take into account the relevant tax implications so as to restore the plaintiff to the position it would have been in had the relevant breach or tortious conduct not occurred.

The relationship between taxation and damages awarded for the loss of future earnings was established in *British Transport Commission v. Gourley*.⁵⁹ It was held that the award of damages should reflect the deductions that would have been made for tax and national insurance in arriving at the settlement figure, because 'to ignore the tax element at the present day would be to act in a manner which is out of touch with reality'.⁶⁰

The Court of Appeal has since affirmed the *Gourley* principle,⁶¹ and it is clear that where damages are awarded for taxable losses (i.e., loss of future income, loss of profits), an income tax or corporate profits tax deduction ought to be made. However, where the damages are meant to compensate for a non-taxable loss (i.e., loss of a capital asset, loss of capital gains), it would be inappropriate to make a deduction for tax as the plaintiff would not have incurred any tax liability thereon.⁶²

55 *Robertson Quay* (No. 2) at [104]–[108].

56 *The Oriental Insurance Co Ltd v. Reliance National Asia Re Pte Ltd* [2009] 2 SLR(R) 385 at [127]–[128].

57 *ibid* at [137]–[138].

58 *ibid* at [129].

59 [1956] AC 185 (HL).

60 *ibid* 203.

61 *Teo Sing Keng and another v. Sim Ban Kiat* [1994] 1 SLR(R) 340.

62 *ibid* 645.

III EXPERT EVIDENCE

i Introduction

The role of expert evidence in legal proceedings is set out in Section 47(1) of the Evidence Act, which establishes that ‘when the court is likely to derive assistance from an opinion upon a point of scientific, technical or other specialised knowledge, the opinions of experts upon that point are relevant facts’.

ii The role of expert evidence in calculation of damages

There is no difference in the principles governing experts in different fields. They all relate to impartiality, and this is reflected in the relevant requirements for expert witnesses outlined in Order 40A of the Rules of Court.

Typically, expert evidence on assessment of damages involves (but is not limited to) issues such as making of assumptions, projection of cash flows and valuation of hypothetical scenarios. Thus, expert evidence usually plays an important role in helping the court understand how each party had derived the figures they have relied upon in their respective cases. The Singapore High Court has stated, in the context of valuation evidence on the valuation of shares, that ‘the court must not defer too readily to expert evidence.... [T]he Court must assess for itself the reasonableness of an expert’s opinion against the criteria of fact and logic. This will sometimes require the court to go deeper into the technical basis upon which the expert valuation has been performed and to consider whether that basis for valuation has been applied using assumptions which are reasonable and justified by the facts’.⁶³

The courts have recognised that an accountant expert may be engaged to fulfil one of at least three roles in connection to litigation. These include: acting as an independent expert and providing an opinion on liability, quantum or both; acting as a consultant assisting in the preparation of the case of one of the litigants; and acting in a supporting administrative role in managing the documentary information required for the litigation. It is only in the first role that the forensic accountant is acting as a forensic expert.⁶⁴ When the accountant acts as a consultant, his or her role is inconsistent with the expert’s duty to be independent – therefore the accountant should not accept a role that requires him or her to be a consultant as well as an independent expert.

iii The court’s role excluding and managing expert evidence

The court’s role in excluding and managing expert evidence is illustrated by Order 25 Rule 3 of the Rules of the Court. In particular, the court will determine, *inter alia*, whether an order should be made limiting the number of expert witnesses;⁶⁵ whether any direction should be made for a discussion between the experts prior to the exchange of their affidavits exhibiting their reports for the purpose of requiring them to identify the issues in the proceedings and where possible, reach agreement on an issue, and if such a direction should be made, whether: (1) to specify the issues which the experts are to discuss; and (2) to direct the experts to

63 *Poh Fu Tek* (No. 38) at [27].

64 *Vita Health Laboratories Pte Ltd and others v. Pang Seng Meng* [2004] 4 SLR(R) 162; [2004] SGHC 158 at [84].

65 Order 25 Rule 3(1)(d) and Order 40A Rule 1.

prepare a joint statement indicating the agreed issues, the issues not agreed and a summary of the reasons for any non-agreement;⁶⁶ and whether directions should be given pursuant to Order 40A.⁶⁷

Where it is apparent that the experts' further assistance is necessary, the courts have seen fit to conduct a hot-tubbing exercise where each expert gives his or her reasons to support his or her conclusions and challenge the opposing expert's conclusions, with the opposing expert having the opportunity to respond immediately. This could be done with the court and counsel asking questions on the reasons and counsel providing facts to support or challenge the reasons given.⁶⁸

Also, in cases where valuation evidence on shares as well as assessment of damages is undertaken, the court has suggested that parties should consider whether the same person should be appointed as the valuer of shares and assessor of damages, to avoid any concern that there may be some discrepancy in the approaches.⁶⁹

iv Independence of experts

The duties of an expert are well summarised in *Ikarian Reefer*,⁷⁰ but probably the most important duty is that of independence. The independence of expert witnesses is governed by Order 40A Rule 2(1), which establishes 'the duty of an expert to assist the Court on the matters within his expertise'. This duty overrides any obligation to the person from whom he or she has received instructions or by whom he or she is paid.⁷¹

There is no overriding objection to a properly qualified person giving expert evidence just because he or she is employed by one of the parties.⁷² The fact of the expert witness' employment may affect the weight of the evidence but that is a separate matter from the question of the expert's independence.⁷³

That being said, when an accountant expert acts as a consultant and assists in the preparation of a party's case, he or she is assisting in the advocacy of the client's case, which is a role that is inconsistent with the expert's need for independence. As such, careful consideration should be accorded to the evidence of an expert accountant who has been engaged as an investigator and collator of facts, and later reprises in court the role of an advocate in support of evidence that he or she has gathered. The courts are cognisant that such evidence may, at times, be coloured by the difficult and sometimes conflicting roles being discharged by the expert accountant.⁷⁴

In addition, the evidence of an expert 'should not only be independent but should also be seen to be independent'.⁷⁵ This means that while the courts will permit a strong defence of an expert's independent views and position, the expert should not stray into engaging in

66 Order 25 Rule 3(1)(f).

67 Order 25 Rule 3(1)(h).

68 *Swiss Butchery* (No. 15) at [114].

69 *ibid* at [112].

70 [1993] 2 Lloyds rep 68.

71 Order 40A Rule 2(2).

72 *Field v. Leeds C.C.* (2000) 32 H.L.R. 618, at 624.

73 *ibid*.

74 *Vita Health* (No. 64) at [84]–[85].

75 *Ku Jia Shiuen (an infant suing through her mother and next friend, Tay Pei Hoon) & Anor v. Government of Malaysia & Ors* [2013] 4 MLJ 108 at [37].

partisan advocacy to advance his or her client's cause.⁷⁶ If he or she appears to do so, his or her independence will be called into question and he or she will inexorably lose credibility.⁷⁷ The expert's advocacy is thus limited to supporting his or her independent views and not the client's cause – this must be brought to the expert's attention by the instructing solicitor.⁷⁸

In addition, in the interests of ensuring that the independence of the expert is preserved, if an expert 'either has or has previously had a significant relationship with any interested party, particulars of this too ought to be disclosed without any prompting. A failure to make proper disclosure in a timely manner may raise serious concerns about apparent or actual bias on the part of the expert'.⁷⁹

Order 40A Rule 3(2)(h) further sets out the requirement for an expert's report to 'contain a statement that the expert understands that in giving his report, his duty is to the Court and that he complies with that duty'. This emphasises that it is to the court that the expert's overriding duty is owed irrespective of who instructed or called the expert.⁸⁰

v Challenging experts' credentials

Per Section 47(2) of the Evidence Act, '[a]n expert is a person with such scientific, technical or other specialised knowledge based on training, study or experience'. There is no need for the expert to be qualified professionally – as long as the court is satisfied that the witness has sufficient knowledge or expertise to qualify as an expert, he or she could be regarded as such.⁸¹ Thus an expert's credentials may be established by his or her experience concerning the matters in question,⁸² so long as the experience relates specifically to those matters.⁸³ Nonetheless, it remains open for any party to challenge an expert's credentials on the basis of his or her lack of professional qualifications or experience, since such matters still affect the weight accorded to the expert evidence.⁸⁴

The expert witness is also required to give details of his or her qualifications in the expert report.⁸⁵ At the very minimum, a curriculum vitae detailing the expert's relevant experience should be provided, with special regard to the issue on which the expert's opinion is sought. The expert's report should state the precise manner, and not merely the general area of inquiry, in which the witness would be of use to the court.⁸⁶ A party may thus use this information as a basis upon which to challenge the expert's credentials.

76 *Resource Piling Pte. Ltd. v. Geospecs Pte Ltd.* [2014] 1 S.L.R. 485 at [103] citing *Pacific Recreation Pte Ltd v. SY Technology Inc* [2008] 2 SLR (R) at [69]–[73].

77 *Pacific Recreation Pte. Ltd. v. SY Technology Inc. and another appeal* [2008] 2 SLR(R) 491; [2008] SGCA 1 at [70].

78 *ibid* at [72].

79 *HSBC Institutional Trust Services (Singapore) Ltd. v. Toshin Development Singapore Pte. Ltd.* [2012] 4 SLR. 738 at [71].

80 Judicial Commissioner Foo Chee Hock, *Singapore Civil Procedure* Volume 2018 Volume 1 (Sweet & Maxwell 2018) at 40A/2/1.

81 *ibid* at 40A/1/2.

82 *Leong Wing Kong v. Public Prosecutor* [1994] 1 SLR(R) 681 at [15].

83 *Singapore Civil Procedure* 2018 (No. 80) at 40A/1/2.

84 *Kong Nan Siew v. Lim Siew Hong* [1971] 1 M.L.J. 262.

85 Order 40A Rule 3(2)(a).

86 *Pacific Recreation* (No. 77) at [67].

vi Oral and written submissions

Unless the court otherwise directs, expert evidence must be given in a written report signed by the expert and exhibited in an affidavit sworn to or affirmed by him or her testifying that the report exhibited is his or hers and that he or she accepts full responsibility for the report.⁸⁷ Such a report must, *inter alia*, give details of the expert's qualifications;⁸⁸ give details of any literature or other material that the expert has relied on in making the report;⁸⁹ contain a statement setting out the issues that he or she has been asked to consider and the basis upon which the evidence was given;⁹⁰ where there is a range of opinion on the matters dealt with in the report, summarise the range of opinion, and give reasons for his or her opinion;⁹¹ and contain a summary of the conclusions reached.⁹²

So, for instance, where damages are to be assessed by reference to a business valuation prepared by an expert witness, the expert should consider the full range of the common methods used in such a valuation (i.e., asset, market and income). Any omission to prepare a valuation on one or more of these methods should be explained in his or her report; likewise, the ultimate choice of valuation should be justified, and where divergent valuations are attained, these should be discussed and explained.

Non-compliance with these requirements does not automatically render the evidence inadmissible.⁹³ However, it may result in the expert's opinion being accorded little or no evidentiary weight as well as in adverse cost consequences for the party who engaged that expert.⁹⁴

IV RECENT CASE LAW

In a landmark decision, the Court of Appeal has affirmed in *Turf Club Auto Emporium v. Yeo Boong Hua*⁹⁵ the availability of *Wrotham Park* damages under Singapore law. Prior to *Turf Club*, references have been made to *Wrotham Park* damages by the Singapore courts,⁹⁶ although such damages have never been awarded. *Wrotham Park* damages are measured (objectively) by such a sum of money as might reasonably have been demanded by the plaintiff from the defendant as a *quid pro quo* for relaxing the covenant between them.⁹⁷ This is akin to a 'licence fee' that the plaintiff could reasonably have extracted in return for his or her consent to the defendant's actions that would otherwise constitute a breach of contract.

In rejecting the restitutionary analysis of *Wrotham Park* damages in favour of the conceptualisation of such damages as compensation for the value of the contractual right

87 Order 40A Rule 3(1).

88 Order 40A Rule 3(2)(a).

89 Order 40A Rule 3(2)(b).

90 Order 40A Rule 3(2)(c).

91 Order 40A Rule 3(2)(e).

92 Order 40A Rule 3(2)(f).

93 *Alwie Handoyo v. Tjong Very Sumito & Anor. and another appeal* [2013] 4 S.L.R. 308 at [173].

94 *Pacific Recreation* (No. 77) at [89].

95 *Turf Club* (No. 12).

96 See *PH Hydraulics & Engineering Pte Ltd v. Airtrust (Hong Kong) Ltd and another appeal* [2017] 2 SLR 129 at [80]; see also *MFM Restaurants* (No. 3) at [55].

97 *Wrotham Park Estate Co Ltd v. Parkside Homes Ltd and Others* [1974] 1 WLR 798 at 815.

that has been breached, the underlying principles of *Turf Club* converge with the recent UK Supreme Court decision in *One Step*,⁹⁸ which sets out the legal position on *Wrotham Park* damages in the United Kingdom.

The Court of Appeal established that the legal requirements for the award of *Wrotham Park* damages under Singapore law are as follows: first, the court must be satisfied that orthodox compensatory damages (measured by reference to the plaintiff's expectation or reliance loss) and specific relief are unavailable; second, it must, as a general rule, be established that there has been (in substance, and not merely in form) a breach of a negative covenant; third, and finally, the case must not be one where it would be irrational or totally unrealistic to expect the parties to bargain for the release of the relevant covenant, even on a hypothetical basis.⁹⁹

This, however, represents a divergence from the UK position regarding the legal requirements of *Wrotham Park* damages. In particular, the Court of Appeal declined to follow the UK Supreme Court in limiting the award of such damages to cases where the contractual right breached is considered to be an economically valuable 'asset' (i.e., where the breach results in the loss of a valuable asset created or protected by the right that was infringed, such as in cases involving a restrictive covenant over land, intellectual property or confidential information).¹⁰⁰ As such, for the purposes of the award of *Wrotham Park* damages under Singapore law, the relevant legal test to be used is the one set out by the Court of Appeal in *Turf Club*, rather than the test adopted by the UK Supreme Court in *One Step*.¹⁰¹

V CIVIL JUSTICE REFORMS

In October 2018, the Ministry of Law in Singapore sought public consultation on civil justice reforms, following the recommendations of the Civil Justice Review Committee (CJRC) and Civil Justice Commission (CJC). By way of context, the CJC was constituted by the Honourable Chief Justice Sundaresh Menon on 5 January 2015 with the mandate to, *inter alia*, 'transform, not merely reform, the litigation process by modernizing it, enhancing efficiency and speed of adjudication and maintaining costs at reasonable levels'.¹⁰² Subsequently, the Ministry of Law announced the establishment of the CJRC on 18 May 2016 to recommend reforms to Singapore's civil justice system. The recommendations made by the CJC and CJRC are wide and far-reaching, ranging from instituting a more judge-driven process in the case management system to an arbitration-style discovery regime to introducing scale costs in litigation. Among the recommendations is one that adopts a default position where a single court expert will be appointed in cases where expert evidence is necessary. The court expert will be granted access to all evidence to assist in the formulation of his or her expert opinion and, generally, no party expert witnesses will be permitted.¹⁰³

The rationale driving the recommendation was that the current system of party appointed experts has its difficulties, namely (1) the expert witnesses often have irreconcilable differences in opinion – their evidence may then unnecessarily complicate the issues before

98 *One Step (Support) Ltd v. Morris-Garner and another* [2018] 2 WLR 1353.

99 *Turf Club* (No. 12) at [217].

100 *One Step* (No. 98) at [92]–[94].

101 *Turf Club* (No. 12) at [283].

102 Civil Justice Commission Report, 29 December 2017, foreword by the Honourable Judge of Appeal Tay Yong Kwang at [1].

103 Report of the Civil Justice Review Committee at [94].

the court, thus becoming counterproductive rather than helpful to the adjudicative process; (2) party-appointed experts are presented with the facts of the case framed according to a particular perspective by the party engaging them, which may influence their interpretation of the evidence; and (3) the disproportionately high costs usually incurred in the preparation and presentation of expert testimony.¹⁰⁴

There is merit in the recommendation as there is much value in having an impartial expert whose paramount duty is to the court, and who has access to all available evidence from both sides to formulate his or her views. It is not uncommon to see party-appointed experts present to the court starkly different opinions, leaving the court with the unenviable task of assessing which of the opinions (if any) to adopt. Under the recommendation, however, the court retains the discretion to allow parties to have their own party-appointed experts in appropriate cases.

104 *Ibid* at [95].

SOUTH AFRICA

*Evert van Eeden and Elzaan Rabie*¹

I OVERVIEW

A breach of contract, a delict or enrichment of one party at the expense of another are the noteworthy events that may entail financial loss for which a judicial award of compensatory damages can be sought within the context of the law of obligations. In the case of infringement of a trademark, damages can be awarded by a High Court. Alternatively, at the request of the proprietor, a reasonable royalty can be awarded in lieu of damages.² As regards damage or loss³ arising from delict, the recovery of compensatory damages will require proof of an act or omission that is ‘wrongful’.⁴ Delictual liability also requires that there must have been fault on the wrongdoer’s part (i.e., either in the form of intention or negligence)⁵ as well as the presence of causation⁶ and harm.⁷ Negligence includes intent in the form of *dolus eventualis*, that is, where a wrongdoer foresees the possibility of a consequence of his or her conduct, but proceeds nonetheless.⁸ Contracts regulate numerous aspects of the relationship between contracting parties, apart from defining their respective duties,⁹ for example limiting or extending liability, imposing penalties or granting indemnities, or providing special methods of settling disputes (e.g., providing for arbitration).¹⁰

State action may constitute a further cause of financial loss for which compensatory damages may be recoverable. Some organs of state¹¹ are clothed with powers by means of

1 Evert van Eeden and Elzaan Rabie are directors at Van Eeden Rabie Inc.

2 Trade Marks Act, 194 of 1993, Section 34(3)(d).

3 See *Jowell v. Bramwell-Jones and others* [2000] 2 All SA 161 (A) 169.

4 Positive conduct that harms the person or property of another is *prima facie* wrongful – *Country Cloud Trading CC v. Member of the Executive Council, Department of Infrastructure Development, Gauteng* 2014 (12) BCLR 1397 (CC) Paragraph 22.

5 *Country Cloud Trading CC v. Member of the Executive Council, Department of Infrastructure Development, Gauteng* 2014 (12) BCLR 1397 (CC) Paragraph 40. See *Kruger v. Coetzee* 1966 (2) SA 428 A 430 as to the test for negligence.

6 Causation posits proof of a causal link between a defendant’s actions or omissions and the harm suffered by the plaintiff, determined on a balance of probabilities – see *Oppelt v. Head: Health, Department of Health, Provincial Administration: Western Cape* 2015 (12) BCLR 1471 (CC) Paragraph 35.

7 *Oppelt v. Head: Health, Department of Health, Provincial Administration: Western Cape* 2015 (12) BCLR 1471 (CC) Paragraph 34.

8 *Country Cloud Trading CC v. Member of the Executive Council, Department of Infrastructure Development, Gauteng* 2014 (12) BCLR 1397 (CC) Paragraph 37 and authorities cited in footnote 38.

9 *ibid.*, Paragraph 63.

10 *id.*

11 Comprehensive procedures must be followed in terms of the Institution of Legal Proceedings against Certain Organs of State Act, 30 of 2002, when an organ of state is cited in legal proceedings.

which persons may be deprived of property, or a liability or administrative penalty¹² may be imposed and assessed.¹³ Examples of such powers wielded by an organ of state are powers in terms of the Income Tax Act,¹⁴ the Expropriation Act,¹⁵ and Section 3(1)(a) and (b) of the Land Reform (Labour Tenants) Act 3 of 1996. Section 25(2)(b) of the Constitution provides that land may only be expropriated subject to compensation – the amount, and the time and manner of payment of which have either been agreed by those affected or decided or approved by a court.¹⁶

An administrative award of ‘damages’ by means of a consent order can be confirmed by the Competition Tribunal or the National Consumer Tribunal. The courts may be called on to review the exercise of their powers by organs of state for a taking of property or an assessment of a liability to make a payment for or for transferring property to the state or to a third party, to determine disputes concerning liability for various forms of loss inflicted or suffered, and to assess the extent thereof. The review of administrative decisions taken by organs of the state is subject to the Promotion of Administrative Justice Act¹⁷ and to the Constitution.¹⁸ Constitutional damages may be awarded by a court as compensation where a breach of administrative justice rights occurs.¹⁹

Arbitration in terms of the Arbitration Act²⁰ plays an important role in commercial disputes. Commercial agreements often contain clauses requiring the resolution of disputes in terms of the Arbitration Act, including the assessment of liability for damages and the assessment thereof. The Supreme Court of Appeal has stated that the onus resting on a party that aims to avoid the consequences of an arbitration clause is not easily discharged.²¹ As the arbitrator is the sole arbiter of fact and law, an arbitrator is not bound by the views of an expert.²² An arbitration award can be rendered binding as an order of court.²³

12 Sections 59(1) of the Competition Act; Section 111 of the Consumer Protection Act, 68 of 2008.

13 Calculation of capital gains tax in terms of the Income Tax Act 58 of 1962 – see *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA).

14 Act 58 of 1962, Section 78(1).

15 Act 63 of 1975.

16 Act 108 of 1996.

17 Act 3 of 2000.

18 Act 108 of 1996.

19 Promotion of Administrative Justice Act, 3 of 2000, Section 8(1)(c)(ii)(bb). The requirements for a claim for Constitutional damages were considered in *Minister of Police v. Mboweni and another* [2014] 4 All SA 452 (SCA), and *Lee v. Minister for Correctional Services (Treatment Action Campaign and Others As Amici Curiae)* 2013 (2) BCLR 129 (CC).

20 Act 42 of 1965.

21 See *De Lange v. Presiding Bishop, Methodist Church of South Africa and another* 2015 1 SA 106 (SCA); *Snowy Owl Properties 284 (Pty) Ltd v. Mziki Shareblock Limited* [2017] JOL 37397 (KZP) Paragraph 17, citing *Zhongji Development Construction Engineering Company Ltd v. Kamoto Copper Company SARL* [2014] 4 All SA 617 (SCA) Paragraph 56.

22 *Municipality v. International Parking Management (Pty) Limited and Others* [2015] JOL 33183 (GSJ) Paragraph 172.

23 Act 42 of 1965 Section 33.

Financial losses that may be the subject of judicial determination and assessment come in many different forms, but only financial loss sustained by a plaintiff with no accompanying physical harm to her person or property²⁴ is referred to as 'economic loss'.²⁵ Conduct causing pure economic loss (as compared to cases of physical harm) is not *prima facie* wrongful.²⁶

Wrongfulness in respect of cases of pure economic loss has been established in a limited number of cases, for example, interference in contractual relations or negligent misstatement.²⁷

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

The judicial determination of liability for, and the assessment of an amount in compensatory damages will often involve the presentation of factual evidence as well as of expert evidence, in turn requiring the identification, evaluation and management by the court of both hearsay and opinion evidence.

ii Evidence

English law has not only been the main source of South Africa's law of evidence,²⁸ but South African law has also been influenced by English law relating to expert evidence. The South African courts have frequently cited the resume of principles relating to expert evidence set out by Cresswell J in the Commercial Court of the Queen's Bench division in *The Ikarian Reefer* and endorsed by the Court of Appeal²⁹ in *National Justice Compania Naviera SA v. Prudential Assurance Co Ltd*.³⁰ In *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another*,³¹ the Supreme Court of Appeal also referred with approval to the passage from the judgment of Justice Marie St-Pierre in *Widdrington* regarding the weight to be accorded to expert testimony.³² A court is entitled to reject a valuation if it is not satisfied with its underlying investigations.³³ An expert witness' expertise must evidence a

24 *Country Cloud Trading CC v. MEC, Department of Infrastructure Development* 2015 (1) SA 1 (CC) A Paragraph 22.

25 *Pillington Brothers (SA) (Pty) Ltd v. Lillicrap, Wassenaar and Partners* [1983] 3 All SA 111 (W) 116.

26 See also *Doug Parsons Property Investments (Pty) Ltd v. Erasmus De Klerk Inc* 2015 (5) SA 344 (GJ) Paragraph 20; *Home Talk Developments (Pty) Ltd and Others v. Ekurhuleni Metropolitan Municipality* 2018 (1) SA 391 (SCA).

27 *Country Cloud Trading CC v. Member of the Executive Council, Department of Infrastructure Development, Gauteng* 2014 (12) BCLR 1397 (CC) Paragraph 24.

28 See *Savoi and others v. National Director of Public Prosecutions and another* 2014 (5) BCLR 606 (CC) Paragraph 37.

29 1993 2 Lloyd's Reporter 68 (QB).

30 Court of Appeal (Civil Division) [1995] 1 Lloyd's Rep 455.

31 [2015] 2 All SA 403 (SCA).

32 *PricewaterhouseCoopers Inc and Others v. National Potato Co-operative Ltd* 2004 (9) BCLR 930 (SCA) Paragraph 99.

33 *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA) Paragraph 28.

cogent scientific basis.³⁴ Contracting parties may agree on terms providing for the method of calculating damages in the event of a breach of contract by one of the parties, or rely on the rules of the common law for the calculation of damages.³⁵

iii Date of assessment

Delictual damages are ordinarily measured as at the date of the delict.³⁶ As a general rule, damages arising from breach of contract are to be calculated as at the time performance was due, or at the date of the breach.³⁷ The time for assessment of damages may be at the latest stage in proceedings when new evidence may still be submitted.³⁸

iv Financial projections

Financial projections may entail a wide array of accounting and actuarial calculations and methodologies. Property, asset and liability valuations may be required, cash flow and capital expenditure forecasts calculated, appropriate discount rates selected, and risk factors considered.³⁹ Calculations must depart from an appropriate and correct database that includes correct and relevant factual evidence and data. The proper assumptions must be made and the correct methodology must be applied. The requirement that a judge must be satisfied with the underlying investigations for any calculation (and for that matter including any financial calculations) remains valid and important,⁴⁰ as does the requirement that an expert witness's expertise must evidence a cogent scientific basis.⁴¹ Material shortcomings in the reliability of the projected capital expenditure (or any other variable) may render the expert's calculations defective.⁴² In *Stepney*, the Supreme Court of Appeal, relying on a passage from Lord Denning's judgment in *Dean v. Prince*,⁴³ observed that a court is entitled to reject a valuation if it is not satisfied with the investigations underpinning it.⁴⁴

34 *Ntsele v. MEC for Health, Gauteng Provincial Government* [2013] 2 All SA 356 (GSJ) Paragraph 92.

35 *Consolidated Rock Machinery Consolidated (Pty) Ltd t/a Bobcat SA v. Mechanical Cleaning Services CC & another* [2006] JOL 17621 (T) Paragraph 13.

36 *Philip Robinson Motors (Pty) Ltd v. N. M. Dada (Pty) Ltd* 1975 (2) SA 420 (A.D.) 28. The Appellate Division is now referred to as the Supreme Court of Appeal.

37 GB Bradfield, *Christie's Law of Contract in South Africa*, 7th ed (2016) 657.

38 JM Potgieter, L Steynberg and TB Floyd, *Law of Damages*, 3rd ed, Juta (2012) 92.

39 See *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA), Paragraph 22.

40 *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA) Paragraph 28.

41 *Ntsele v. MEC for Health, Gauteng Provincial Government* [2013] 2 All SA 356 (GSJ) Paragraph 92.

42 See *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA).

43 [1954] 1 All ER 749 at 758: 'For instance, if the expert added up his figures wrongly, or took something into account which he ought not to have considered, or conversely, or interpreted the agreement wrongly, or proceeded on some erroneous principle in all these cases, the court will interfere.'

44 *Commissioner for the South African Revenue Service v. Stepney Investments (Pty) Ltd* [2016] 1 All SA 1 (SCA) Paragraph 28.

v Assumptions

The factual evidence presented to the court lays the groundwork for the expression of an opinion and the opinion must be relevant to the factual evidence. An unfounded or unrealistic assumption (for example, an assumption not based on factual evidence or that is tainted by hearsay or an incorrect hypothesis) may have the effect of contaminating expert evidence.⁴⁵ Assumptions should be ‘sound’ and the court may accept actuarial assumptions.⁴⁶

vi Discount rates

The applicable discount rate, inflation rate and life expectancy are actuarial issues to be determined or agreed by the actuaries.⁴⁷

vii Currency conversion

Where a debt obligation is expressed in a foreign currency, the question to be considered is whether the debtor has responded in terms of the agreement and has paid to the creditor the equivalent of the expressed amount in rand, and, if so, the debt is satisfied.⁴⁸

viii Interest on damages

Where the parties to a contract have not agreed on an interest rate at which an amount payable under an agreement is to be calculated, this does not render the agreement invalid. The interest rate prescribed from time to time by notice in the Gazette in terms of the Prescribed Rate of Interest Act⁴⁹ will apply if no rate has been agreed between the parties (provided that the interest rate is not governed by another law).⁵⁰ A court may (subject to any other agreement between the parties⁵¹ and the provisions of the National Credit Act⁵²) grant an order that interest on the judgment amount shall run from a date determined by the court. The court making a finding of damages may give judgment to be calculated on the amount awarded at the rate of interest prescribed in terms of the Prescribed Rate of Interest Act. Unless expressly agreed by the parties to a contract, interest will be payable calculated as simple interest and not as compound interest.⁵³ The rate of interest prescribed in terms of the Prescribed Rate of Interest Act is periodically adjusted and is typically below the prime rate of interest.

45 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* [2015] 2 All SA 403 (SCA) Paragraph 118.

46 *Oosthuizen v. Member of the Executive Council & another* [2006] JOL 18165 (T); *Nienaber v. RAF* [2012] JOL 28355 (GSJ) Paragraph 4.

47 See *Reay and another v. Netcare (Pty) Ltd t/a Umblanga Hospital and Others* [2016] 4 All SA 195 (KZP) Paragraph 53, where the trial judge, in the context of an agreement between the parties as to a claim for loss of support, was requested by the parties to determine the basis of the calculations pertaining to the loss of support to enable the actuaries to determine the loss and to give directions and specify relevant assumptions.

48 *Zelenyck v. Avnit* [2009] JOL 23748 (GNP).

49 Act 55 of 1975.

50 See *Basson and others v. Hanna* 2017 (3) SA 22 (SCA) Paragraph 16.

51 See JM Potgieter, L Steynberg and TB Floyd, *Law of Damages*, 3rd ed, Juta (2012), 205.

52 Act 34 of 2005.

53 *Euro Blitz 21 (Pty) Ltd and another v. Secena Aircraft Investments CC* [2015] JOL 32990 (SCA).

ix Costs

A party that is successful in a claim (or defence) is normally entitled to its costs on a party and party scale (as opposed to attorney and client costs, which reflect the attorney's fees charged to his or her client). The court does, however, have discretion to deprive a successful party partially or entirely of its costs, and, even, to make an order requiring the successful party to pay the unsuccessful party's costs.⁵⁴

x Tax

The relevant tax table applicable for each year applies.⁵⁵

III EXPERT EVIDENCE

i Introduction

There may be cases where the court is, by reason of a lack of special knowledge and skill, not sufficiently informed to enable it to undertake the task of drawing properly reasoned inferences from the facts established by the evidence.⁵⁶ Addressing the role of an expert, the court in *Schneider NO and Others v. AA and another*⁵⁷ refers to the South African Law of Evidence,⁵⁸ citing the well-known passage from *National Justice Compania Naviera SA v. Prudential Assurance Co Ltd (The Ikarian Reefer)* [1993] 2 Lloyd's Rep 68 at 81, setting out the duties of an expert witness.⁵⁹

Not all hearsay evidence is necessarily inadmissible,⁶⁰ and not all hearsay evidence will necessarily amount to expert evidence.⁶¹ As described by the former Appellate Division (now the Supreme Court of Appeal) in *Coopers (South Africa) (Pty) Ltd v. Deutsche Gesellschaft für Schädlingsbekämpfung MBH*, an expert's opinion represents his or her reasoned conclusion based on certain facts or data, which are either common cause, or which are established by his or her own evidence or that of some other competent witness.⁶² An expert's bald statement of his or her opinion (except possibly where it is not controverted) is, however, not of any real

54 *Michael and another v. Linksfield Park Clinic (Pty) Ltd and another* 2001 (3) SA 1188 (SCA) Paragraph 5.

55 See *Reay and another v. Netcare (Pty) Ltd t/a Umhlanga Hospital and others* [2016] 4 All SA 195 (KZP) Paragraph 53.

56 *Coopers* 370. See generally M Dendy et al 'Evidence' 'Expert evidence' LAWSA 3rd ed Vol 18. 2010 (5) SA 203 211.

57 Zeffertt, Paizes and Skeen, *The South African Law of Evidence*, Second Edition (2009), LexisNexis 330.

59 The Supreme Court of Appeal in *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* [2015] 2 All SA 403 (SCA) Paragraph 99 also cites with approval the judgment of Justice Marie St-Pierre in *Wightman v. Widdrington* (Succession de) 2013 QCCA 1187 (CanLII).

60 For the factors that the court may consider in determining whether hearsay evidence should be admitted, see Section 3 of the Law of Evidence Amendment Act 45 of 1988 and the discussion thereof by DT Zeffertt and AP Paizes, *The South African Law of Evidence*, 2nd ed, LexisNexis (2009) 389.

61 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* [2015] 2 All SA 403 (SCA) Paragraph 96.

62 1976 (3) SA 370.

assistance – proper evaluation of the opinion can only be undertaken if the process of reasoning that led to the conclusion, including the premises from which the reasoning proceeds, are disclosed by the expert.⁶³

ii The role of expert evidence in calculation of damages

As noted by Davis J in *Schneider NO and Others v. AA and another*, an expert comes to court to give the court the benefit of his or her expertise; while an expert is called by a particular party (presumably because the conclusion of the expert, using his or her expertise, is in favour of the line of argument of the particular party) this does not absolve the expert from providing the court with as objective and unbiased an opinion, based on his or her expertise, as possible.⁶⁴ An expert must not be a hired gun who dispenses his or her expertise for the purposes of a particular case, and should not assume the role of an advocate, nor give evidence that goes beyond the knowledge he or she claims to possess.⁶⁵

In considering various, and often conflicting expert opinions, as a rule, a court must make a determination of reasonableness⁶⁶ and negligence not by reference to considerations of credibility, but by examining the opinions and analysing their essential reasoning, in preparation for the court reaching its own conclusion of the issues raised.⁶⁷ What is thus required of the trial judge is to determine to what extent the opinions advanced by the experts are founded on logical reasoning and how the competing sets of evidence stand in relation to one another, viewed in the light of the probabilities.⁶⁸

iii The court's role excluding and managing expert evidence

It has been said that the integrity of the justice system is anchored in the impartiality of the judiciary, which should refrain from descending into the arena.⁶⁹ The judge nevertheless has the power to control trial proceedings to ensure that they are conducted in a manner that avoids delay and the unwarranted escalation of costs. The court may question a witness' expertise *mero motu* or at the behest of a party. Notwithstanding the fact that the conduct of a trial is largely a matter for the parties to determine as they present their cases, the judge may make rulings regarding the presentation and admissibility of hearsay evidence.⁷⁰ The court will be loath to interfere with the parties' management of the matter. The Supreme Court of Appeal has noted that,⁷¹ while provisionally admitting expert evidence of limited scope where its admissibility is contestable, such a practice in relation to a matter of larger

63 *Coopers (South Africa) (Pty) Ltd v. Deutsche Gesellschaft Für Schädlingsbekämpfung MBH* 1976 (3) SA 352 (A) 371.

64 2010 (5) SA 203 (WCC) 211-212.

65 2010 (5) SA 203 (WCC) 212.

66 That is to say, the 'reasonableness of imposing liability' – see *Masstores (Pty) Ltd v. Pick N Pay Retailers (Pty) Ltd* 2017 (1) SA 613 (CC) Paragraph 48.

67 *Michael and another v. Linksfield Park Clinic (Pty) Ltd and another* 2001 (3) SA 1188 (SCA) Paragraph 34.

68 *Louwrens v. Oldwage* [2006] 1 All SA 197 (SCA) Paragraph 27.

69 *S v. Le Grange* 2009 (1) SACR 125 Paragraph 21, cited in *City of Johannesburg Metropolitan Council v. Ngobeni* [2012] JOL 29134 (SCA) Paragraph 31-33.

70 In *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 434-435.

71 2015] 2 All SA 403 (SCA) 434.

scope and magnitude may have disastrous consequences.⁷² It is consequently incumbent upon judges hearing cases of substantial potential magnitude to exercise control over the conduct of proceedings to prevent the proceedings from assuming unmanageable proportions, since overuse of scarce judicial resources would be to the detriment of both the parties and society.⁷³

iv Independence of experts

Any fact that may compromise the independence of an expert witness should be disclosed to the court.⁷⁴ A party who has an interest in a matter by, for example, being a funder of one of the litigants should not be represented as being an independent or disinterested expert in the case.⁷⁵ A party may, for example, be admitted as an *amicus curiae*, in which event the court would be apprised of the nature and purpose of the party's participation in the matter.⁷⁶

v Challenging experts' credentials

The differentiation between factual, expert and hearsay evidence is fundamental to the orderly and fair conduct of a trial, and, if done incorrectly, may have fateful consequences for the outcome. The challenging of an expert's credentials can be undertaken both during preparation for trial and during the trial, and, depending on the nature of the challenge, either by a party or the judge. The primary pretrial mechanism for challenging an expert's credentials is embodied in Rule 36(9) of the Uniform Rules of Court. Save with the leave of the court or with the consent of all the parties, a party who intends to present a witness to give expert evidence must, at least 15 days before the hearing, deliver a notice of his or her intention to do so,⁷⁷ and must, at least 10 days before the hearing, furnish the other party with a 'summary' of the witness's opinions and his or her reasons therefor.⁷⁸ These periods will often be inadequate in practice and extended periods may be required, failing which trials may not be ready for hearing.⁷⁹ A challenge to an expert's credentials or to the procedure adopted for the presentation of expert evidence at the trial can be made at the pretrial conference, which must be held in terms of Rule 37 of the Uniform Rules of Court, alternatively by means of an interlocutory application, as a point *in limine*, or during the trial itself. Grounds on which the evidence of an expert witness can be challenged include failure to comply with the provisions of Rule 36(9); an objection that a witness is not an expert where expert opinion is required on a specified matter; an objection that a particular witness is not an expert witness for the purpose of testifying as to the subject matter of the evidence summarised in the Rule 36(9) summary;⁸⁰ and an objection

72 In *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 78.

73 *ibid.*, Paragraph 161.

74 *Schneider NO and others v. AA and another* 2010 (5) SA 203 (WCC) 220. See also *Menday v. Protea Assurance Co Ltd* [1978] 1 All SA 535 (E).

75 *Schneider NO and others v. AA and another* 2010 (5) SA 203 (WCC) 220. *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another*.

76 *Schneider NO and Others v. AA and another* 2010 (5) SA 203 (WCC) 220.

77 Uniform Rules of Court Rule 36(9)(a); *Coopers (South Africa) (Pty) Ltd v. Deutsche Gesellschaft Für Schädlingsbekämpfung MBH* 1976 (3) SA 352 (A) Paragraph 370.

78 Uniform Rules of Court Rule 36(9); *Coopers (South Africa) (Pty) Ltd v. Deutsche Gesellschaft Für Schädlingsbekämpfung MBH* 1976 (3) SA 352 (A) Paragraph 370.

79 See the practice directions for the various courts.

80 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 101.

that evidence will be or has been presented falls beyond the scope of the summary.⁸¹ In order to avoid burdening the court, it is of fundamental importance that possible hearsay evidence or non-expert evidence be identified and challenged as soon as possible.⁸²

Characterising the nature of evidence called or proposed and challenging an expert's credentials at an appropriate time are important in balancing the freedom of the parties to determine the conduct of the trial against the need for the judge to intervene in proceedings to ensure that they are conducted in a manner that avoids delay and unwarranted escalation of costs.⁸³ The Supreme Court of Appeal in *PricewaterhouseCoopers*⁸⁴ observed that the basic principle of trial practice regarding the calling of witnesses of fact and expert witnesses is that, while a party may generally call its witnesses in any order it likes, it is the usual practice for expert witnesses to be called after witnesses of fact, 'where they are to be called upon to express opinions on the facts dealt with by such witnesses'.⁸⁵ This practice necessitates identification and characterisation at the earliest possible opportunity of evidence that is being presented to the court. If factual evidence is presented under the guise of expert evidence, it may eventually cause grave problems for the conduct of the trial and the determination of the dispute.

In *PricewaterhouseCoopers*, the Supreme Court of Appeal held that it should have become clear within a few days of the plaintiff's main witness commencing to give evidence that such evidence was 'overwhelmingly based upon hearsay'. The first course open to the judge (at the commencement of the trial) was to require the plaintiff to identify the hearsay evidence that it wished to have admitted and to make application for its admission on any available ground, and then to make a ruling on its admissibility.⁸⁶ Insofar as it had been indicated that a witness would be called upon to substantiate such hearsay evidence, the second course open to the judge would have been to require that the evidence of the main witness stand down until such (factual) evidence had been presented and was properly before the court. The next stage at which the matter of the characterisation and admissibility of evidence could have been addressed was on completion of the witness' evidence and prior to his cross-examination. The witness should not, therefore, have been cross-examined on the evidence that was arguably inadmissible.⁸⁷ It was only at the end of a trial of considerable length that the evidence of the witness was challenged as being of an inadmissible hearsay nature. 'By then of course it was impossible to sort the wheat of admissible evidence from the chaff of inadmissible hearsay.'⁸⁸

It is not necessary that the grounds on which the expertise of the expert witness is based must be set out in the Rule 36 Notice. The court must, however, be satisfied as to the expertise of an expert witness.⁸⁹ While Rule 36(9) does not require that exposition of the expert's expertise must be set out in the Rule 36(9) notice, a party that fails to address the expert's

81 See generally P van den Heever *Objections in Civil Litigation* Juta (2010) 67.

82 See *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 158 – 159.

83 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* [2015] 2 All SA 403 (SCA) Paragraph 160.

84 Citing Tristram Hodgkinson *Expert Evidence : Law and Practice* 106–7.

85 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another*, Paragraph 80.

86 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 80.

87 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 81.

88 *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 81.

89 *Consolidated Rock Machinery (Pty) Ltd t/a Bobcat SA v. Mechanical Cleaning Services CC & another* [2006] JOL 17621 (T) Paragraph 20.

expertise in the notice renders itself vulnerable to a challenge both by the court and the other party, as such lacking information renders it impossible to assess whether the witness will be qualified to give the evidence described in the summary in terms of Rule 36(9). The main purpose of Rule 36(9) is to require the party intending to call a witness to give expert evidence to give the other party such information about the evidence as will remove the element of surprise, something that was viewed as tending to cause delay in the conduct of trials.⁹⁰ The draughtsman of the summary (facts and data) should, therefore, ensure that no information is omitted, where the omission thereof might lead to the other side being taken by surprise when in due course such information is adduced in cross-examination or evidence.⁹¹ Proper compliance with the sub-rule is perceived as enabling experts to exchange views before giving evidence and thus to reach agreement on at least some of the issues, thereby saving costs and the time of the court.⁹²

vi Novel science and methods

It is an established principle that courts and arbitrators are not bound by the opinions of experts.⁹³ As stated in *Municipality v. International Parking Management*, the court remains the sole arbiter of fact and expert evidence must be weighed up, accepted or rejected by the court in the same way as any other evidence. Satchwell J in *Holtzhauzen v. Roodt*⁹⁴ (cited in *Municipality v. International Parking Management*)⁹⁵ cautions that ‘opinion evidence must not usurp the function of the court. The witness is not permitted to give opinion on the legal or the general merits of the case. The evidence of the opinion of the expert should not be proffered on the ultimate issue’. Whether science and methods that form the subject of expert evidence are novel or not is not the determining factor, but whether the expert evidence of the witness falls within the legitimate bounds of the testimony of an expert witness.

vii Oral and written submissions

The Supreme Court of Appeal has emphasised that an expert may be tendered for cross-examination upon his or her report alone, without additional oral examination, or after only limited questioning, and that, as a rule, the report of an expert witness can be read as the evidence in chief, subject only to supplementary questions necessary for explanation or elaboration of the report.⁹⁶ Ultimately, it remains for the court to evaluate the testimony that is presented as expert evidence.

90 *Consolidated Rock Machinery (Pty) Ltd t/a Bobcat SA v. Mechanical Cleaning Services CC & another* [2006] JOL 17621 (T) 17.

91 *id.*

92 See *Klue and another v. Provincial Administration*, Cape 1966 (2) SA 561 (E) 563, cited in *Consolidated Rock Machinery* 17.

93 *Municipality v. International Parking Management (Pty) Limited and Others* [2015] JOL 33183 (GSJ) Paragraph 172.

94 1997 (4) SA 766 (W) at 773.

95 *Municipality v. International Parking Management (Pty) Limited and Others* [2015] JOL 33183 (GSJ) Paragraph 171.

96 See *PricewaterhouseCoopers Incorporated and others v. National Potato Co-operative Ltd and another* Paragraph 161 and sources cited there.

IV RECENT CASE LAW

i Breach of contract

The remedies available for a breach have been set out in *Christie's Law of Contract in South Africa*.⁹⁷ These remedies are specific performance, interdict, declaration of rights, cancellation and damages. The choice among these remedies rests primarily with the injured party, the plaintiff, who may choose more than one of them. The plaintiff's choice is subject to the overriding principles that it must not claim inconsistent remedies and must not be overcompensated. The traditional view that a party who is, *prima facie*, entitled to specific performance may claim in the alternative damages as surrogate for specific performance held sway until the judgment in 1981 in *Isep Structural Engineering and Plating (Pty) Ltd*.⁹⁸ The Supreme Court of Appeal has now made it clear that, save in relation to instances of leases and the obligation of reinstatement under a lease where the law as set out in *Isep* still applies, the remedy of damages in lieu of specific performance will be available to a plaintiff where specific performance by the defendant is no longer possible.⁹⁹

ii Breach of fiduciary duty

A plaintiff who takes legal action claiming for loss or damage arising from breach of a fiduciary duty must plead causation and allege a link between the wrongful act (the breach of fiduciary duty) and the damage, where the former caused the latter.¹⁰⁰

97 GB Bradfield 7th ed (2016) 616. See *Basson and Others v. Hanna* 2017 (3) SA 22 (SCA) Paragraph 22.

98 1981 (4) SA 1 (A).

99 See *Basson and Others v. Hanna* 2017 (3) SA 22 (SCA).

100 *Du Plessis NO v. Phelps* [1995] 2 All SA 469 (C) 475. See also *Symington and others v. Pretoria-Oos Privaat Hospitaal Bedryfs (Pty) Ltd* [2005] 4 All SA 403 (SCA); *Derbigum Manufacturing (Pty) Ltd v. Callegaro and Others* [2014] JOL 31495 (GSJ) 9.

SPAIN

Alex Ferreres Comella and Cristina Ayo Ferrándiz¹

I OVERVIEW

Proving the existence and the amount of actual damages resulting from somebody else's acts or behaviour is an essential requirement for any compensatory claim that is filed with the Spanish courts. Thus, Spanish tort law is based on the principle that no legal action for compensation can be brought in the absence of actual damage.

Therefore, the standard of proof on the (1) existence of the claimed damages (2) their exact calculation and (3) their causal relationship with the wrongdoing or act that caused the damages is high. The claimant is expected to provide the court with documentary evidence that supports the existence of direct damages and expert witness evidence on the calculation of their monetary value and on the existence and calculation of loss of profit. Punitive damages are not available under Spanish law, but only compensation for damages (aimed at restoring the aggrieved party to the financial position he or she was in before the act that caused the damages took place) is awarded.

Damages that can be claimed include both pure financial damages, and pain and suffering (which are referred to as moral damages under Spanish law).

Claiming damages normally involves requesting monetary compensation. Nevertheless, nothing in Spanish tort law prevents a claimant from requesting an *in natura* restoration instead of monetary compensation. Thus, for example, a claimant who claims pain and suffering (in the form of anxiety) as a consequence of his or her fear of suffering future personal injuries as a result of his or her exposure to a defective product that is proven to potentially cause such injuries may be entitled to request the manufacturer of the defective product to pay for periodic medical checks for him or her to alleviate such anxiety. Restoration *in natura*, though, is very exceptionally applied, and monetary compensation is more common.

As to the scope of damages that the claimant can claim, there is no specific regulation on remoteness under Spanish law. However, though this is limited to contract liability, the Spanish Civil Code sets out that a good faith debtor will only be liable for damages that he or she could have reasonably expected the counterparty would suffer as a consequence of the debtor not fulfilling his or her obligations. Bad faith debtors (which under Spanish case law includes both debtors who willingly breach the contract and debtors who when the contract was executed should have considered the possibility that they would not be able to honour their contractual obligations) are responsible for all the damages – both direct and indirect – that derive from their acts or behaviour, without limitation.

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There is no equivalent rule for non-contractual liability, but according to most scholars and case law, a mere negligent tortfeasor is equivalent to a good faith debtor, while a grossly negligent and intentional tortfeasor is equivalent to a bad faith debtor.

The obligation of the aggrieved party is to mitigate the damages suffered, thus he or she must make reasonable efforts to limit additional losses.

Compensation rights are subject to a five-year limitation period in the case of contractual damages and to a one-year limitation period for non-contractual damages. However, in relation to non-contractual damages, some laws state otherwise (e.g., the Spanish product liability regulation provides a three-year limitation period).

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

As mentioned above, quantifying financial loss (which entails both proving that the financial damages claimed actually exist and have already accrued) is critical to be able to claim damages.

As regards contractual liability, the high standard of proof on the existence and amount of damages has led to a widespread inclusion of penalty clauses in contracts. Thus, through the penalty clauses, parties establish the monetary value of the damages that a breach of contract by either party will cause the other party. In the event of a breach of contract, the non-breaching party can directly claim the amount established in the penalty cause, without having to prove causation and the monetary value of the damages actually suffered.

Penalty clauses are mainly used in contracts to relieve the aggrieved party from the burden of having to prove the loss of profits resulting from the breach of contract. The Spanish Supreme Court has recently confirmed the validity of penalty clauses included in contracts and the inability of courts to not apply or to only partially apply these clauses when the breach of contract established in the clause has occurred. Only very exceptionally, in the cases in which the defendant proves – on the basis of hardship theories – that the penalty clause greatly exceeds the actual damages suffered, can the court possibly reduce the amount of the penalty.

Finally, it is worth noting that when the financial loss to be calculated arises from personal injury, courts tend to apply by analogy the compensation schedules set out in Law 35/2015 for the calculation of damages in motor vehicle accidents. As a result, court-awarded compensation in Spain is lower than in other jurisdictions.

ii Evidence

The claimant must provide evidence of the existence and amount of the claimed damages. The means of evidence available to the aggrieved party to prove the existence and the amount of damages are:

- a* inspection of the damaged assets or the personal injuries by the court; this is an important means of evidence in very limited cases where it is used as a source of evidence that supplements expert witness evidence on the damages;
- b* documentary evidence; it is relevant in connection with direct damages that involve costs incurred by the aggrieved party. Documentary evidence is also relevant in connection with medical history when damages arising from personal injuries are claimed. Furthermore, documentary evidence may be relevant as supporting expert witness assumptions when calculating loss of profits;

- c expert witness; expert reports are specifically relevant for the calculation of damages, particularly for the calculation of loss of profits. Calculating loss of profits requires expertise in economics, and company finance and accounting; and
- d factual witnesses; this means of evidence is often not sufficient to prove damages.

iii Date of assessment

Direct damages are calculated as per their monetary value from the moment they begin to accrue. When direct damages are projected into the future (e.g., when costs for future medical checks or third-party assistance for people with disabilities are to be considered) or loss of profits are to be calculated, their monetary value is assessed as from the date on which they are presumed to have begun to accrue. For instance, if the aggrieved party who has suffered serious personal injuries is expected to need permanent assistance by a third party or to renew his or her prosthetics from time to time in the future, their monetary value will be assessed taking into account their estimated future cost.

iv Financial projections

Financial projections are made by expert witnesses when calculating loss of profits.

Financial projections involve the application of assumptions related to circumstances such as (1) the evolution of prices or interest rates; (2) life expectancy; (3) the expected length of working life; (4) the expected evolution of a specific market; (5) the expected evolution of the aggrieved party's future income. The correct choice by the expert witness of the source of information to base his or her assumptions on the financial projections is critical.

v Assumptions

With regard to contractual liability, Spanish case law has set a presumption that a breach of contract causes actual damage to the aggrieved party (i.e., it is thus the defendant's burden to prove that the breach of contract did not result in any actual damage to the aggrieved party). Such presumption is not applicable to non-contractual liability.

As regards calculating damages, assumptions by expert witnesses are sometimes inevitable in order to calculate loss of profits, as mentioned above. The Spanish Supreme Court has traditionally required that those assumptions be based on very probable hypotheses (thus certainty is not a requirement).

vi Discount rates

Spanish expert witnesses who calculate loss of profit are familiar with the need to take into account discount rates in connection with future profits that would have been obtained but for the third party's breach of contract or tortious behaviour. However, when acting before the judiciary, Spanish expert witnesses normally limit the scope of the discount rates to those that relate to the time value of money (i.e., the fact that the claimant should not benefit from the fact that he or she will dispose as from the decision of monetary compensation for profits that he or she would otherwise have obtained in the future).

However, experts do not apply additional discount rates related to the residual amount of risk of the future expected profits not finally accrued since Spanish courts have traditionally been very reluctant to award any loss of profit if the claimant cannot clearly prove the more than likely (most probable) accrual of profits had the breach of contract or detrimental action not occurred.

Spanish arbitration courts, however, are more familiar with the application of discount rates related to residual amount of risk of the future expected profits and more frequently accept them, thereby lessening the claimant's burden to prove that the profits would have most probably been made.

vii Currency conversion

Spanish law requires that compensation be paid in national currency (in euros). Any amounts related to the calculation of compensation in a foreign currency must be converted into euros. When the amount to be considered relates to a cost incurred by the aggrieved party as a consequence of the event causing damage, the currency conversion must be carried out applying the exchange rates at the time the direct damage accrues (e.g., when the invoice related to a cost caused by the harmful action is settled).

Because of the uncertainty of future currency conversion rates, courts do not take into account the risk of devaluation or the benefit of revaluation of currency as regards compensation for loss of profits (i.e., for profits that would have been made in the future had the action that caused the damage not occurred) when the conversion is made.

viii Interest on damages

In relation to contractual liability, claimants are entitled to claim interest on damages.

In the absence of an agreement between the parties on the interest rate to be applied to a breach of contract, legal interest rates apply. Interest rates accrue as from the moment the obligation becomes due (if so stated in the contract) or as from the moment the claimant formally requests payment from the debtor.

Once the claim for damages is filed with the courts, the claimant is awarded 2 per cent interest on the legal interest on the amount awarded by the court until the defendant pays in full.

In non-contractual liability cases, the aggrieved party is entitled to request interest on damages as from the moment the damages begin to accrue. As with contractual liability, once the claim is filed with the courts, a 2 per cent rate on the legal interest applies.

ix Costs

The aggrieved party can claim costs incurred as a consequence of the act that caused the damage or behaviour of the counterparty or tortfeasor. The costs include direct and indirect costs. As regards indirect costs, however, theories such as remoteness are available to defendants in Spain to try to limit the scope of the indirect damages to be compensated.

According to the duty to mitigate rule, the aggrieved party must try to find the most economical way in the market to restore the situation or mitigate the damage.

When the costs incurred by the aggrieved party include variable costs (in particular, the costs of producing assets), expert evidence by a specialist accountant may be effective.

x Tax

The tax that the aggrieved party would have paid as a result of the profits that he or she would have obtained but for the other party's breach of contract or the tortfeasor's act or activity are not taken into account for the purposes of calculating compensation. In the same vein,

taxes that the aggrieved party would not have paid had the action that caused the damage not occurred is a direct damage that is taken into account for the purposes of calculating compensation.

III EXPERT EVIDENCE

i Introduction

Expert evidence is expressly allowed in declarative proceedings under the Spanish Procedure Law.

Spain has two basic declarative proceedings to seek the payment of compensation for damages: verbal proceedings and ordinary proceedings. Which proceedings apply in each case depends on the amount claimed: (1) verbal proceedings apply in cases involving compensation up to €6,000; (2) ordinary proceedings apply in cases involving compensation exceeding €6,000.

In both cases, the proceedings begin with the filing of the claim, which must include the facts of the case and the legal grounds on which the claim is based. In both cases, any documentary evidence and expert reports available on the facts or events on which the allegations are based should to be attached to the briefs filed with the court. Note that no other documents will be accepted at a later stage, except in exceptional circumstances, as explained below.

If verbal proceedings are initiated, once the claim is filed and given leave to proceed, the defendant is notified so that he or she may present a defence within 10 working days (which include every day of the year except Saturdays, Sundays, national holidays, non-working days in the autonomous region in question or city where the proceedings are held, and the month of August). This period cannot be extended unless the parties agree to stay the proceedings.

Subsequently, the court will call the parties to a hearing in which the parties propose evidence, it is examined and the final conclusions are presented.

If ordinary proceedings are initiated, once the lawsuit is notified, the defendant will have 20 working days to file the brief of response. This period cannot be extended unless the parties agree to stay the proceedings.

Subsequently, the court will call the parties to a preliminary hearing in which they will propose evidence and, finally, the court will call the parties to the trial where the evidence and final conclusions are presented.

ii The role of expert evidence in calculating damages

No particularities exist in the Spanish Procedure Law regarding experts that lead with the calculation of damages. However, according to standard practice, the following differences can be highlighted:

- a* in cases involving insurance coverage, an expert to investigate the cause of the accident other than the one who calculates the damages caused as a result of the accident may be proposed;
- b* in cases involving construction defects, the same expert usually handles both tasks;
- c* finally, in cases involving breaches of contract, normally no expert is proposed to investigate the cause of the breach, since this point requires a legal analysis. Thus, in these cases, expert opinion is normally limited to calculating the damages caused by the breach.

iii The court's role excluding and managing expert evidence

In principle, expert reports should be filed together with the initial briefs of claim and of defence. This means that, as a general rule, the experts are usually appointed by the parties themselves. However, there are a number of exceptions in extraordinary circumstances.

In particular, when there is a risk that the action could expire and, therefore, it is proven that the claimant could not delay filing the claim in order to protect his or her rights, the claimant may submit an expert report at a later stage provided that this is declared in the brief of claim and the report is filed prior to the preliminary hearing.

In turn, given that the defendant only has 20 working days to file the brief of response, the Spanish Procedure Law allows the defendant to file an expert report five days prior to the preliminary hearing, provided that the defendant justifies that the report could not be obtained before the expiry of the term provided by law to file the defence brief and it declares this in his or her brief of response.

Moreover, if the need for expert witness evidence becomes clear in view of the pleadings contained in the defendant's brief of defence, or in view of the additional pleadings made by any of the parties prior to or at the preliminary hearing, the parties may submit any such expert witness report up until five days before the start of the trial.

On the other hand, the parties may prefer to request the court to appoint an expert rather than appoint one themselves. In this case, they should request so expressly in their initial briefs.

Moreover, the appointment of an expert by the court can also be requested when the need for expert testimony becomes evident either in view of the pleadings contained in the writ of defence (in which case it may only be requested by the claimant) or in view of any additional pleadings made by any of the parties before or at the preliminary hearing.

As in the cases where an expert is proposed by the parties, the cost of issuing a court-appointed expert report is assumed by the party that requested such appointment.

iv Independence of experts

Regardless of whether the experts are proposed by the parties or appointed by the court, pursuant to the Spanish Procedure Law, all experts must state under oath or affirmation and act as objectively as possible, taking into consideration both what may favour or what may harm the parties, that they are aware of the penalties they could face for failing to do so.

v Challenging experts' credentials

When the expert is proposed by one of the parties, and the report is attached to the brief of allegations, the expert is expected to have specific knowledge of the matter of the opinion.

If the expert is appointed by the court, he or she should have an official title corresponding to the matter and nature of the opinion or report. If there is no official professional title for the matter, the experts appointed must have good knowledge of the matter.

Pursuant to the Spanish Procedure Law, the opinions of academics, cultural and scientific institutions that study the subject matter of the expert opinion or of duly qualified legal persons are also valid.

Taking into consideration that the general rule is that experts be appointed by the parties, pursuant to the Spanish Procedure Law, only court-appointed experts can be objected to and disqualified.

In turn, the experts proposed by the parties can be challenged in any of the following circumstances:

- a* if they are a spouse or a relation up to the fourth degree of consanguinity or affinity of one of the parties, their lawyers or court agents;
- b* if they have a direct or indirect interest in the matter or in another similar matter;
- c* if they are or have been in a situation of dependency or conflict of interest with either of the parties, their lawyers or court agents;
- d* if they are close friends or hostile towards either of the parties, their lawyers or court agents; or
- e* if there is any other duly evidenced circumstance that makes them professionally unsuitable.

Moreover, and unless otherwise agreed by the parties, the opinion of an expert who has been involved in mediation or arbitration proceedings concerning the matter at hand is not valid.

vi Novel science and methods

Whenever novel science is involved and no personal expert is available, as mentioned above, the opinions of academics, cultural and scientific institutions that study the subject matter of the expert opinion or of duly qualified legal persons are also valid.

vii Oral and written submissions

As explained above, expert reports must be proposed and submitted by parties in their respective briefs of allegations. Only in the following exceptional circumstances can they be submitted later:

- a* Owing to reasons of lack of time, the parties may announce in their briefs of allegations (claim and defence) that the report will be attached at a later stage. In this case, the report must be submitted five days prior to the preliminary hearing.
- b* As a consequence of the allegations made by the defendant in his or her defence brief, or if new facts arise, or as a result of additional allegations made by the parties before or during the preliminary hearing.
- c* When a request that the expert report be expanded on is made (during the hearing).
- d* Moreover, a party can request the court to appoint an expert:
 - when a party waives its right to appoint an expert in the brief of allegations and requests the court to do so; and
 - as a consequence of the allegations made by the defendant in its brief of defence, if new facts arise or as a result of additional allegations made by the parties before or during the preliminary hearing.

Either upon attaching the expert report to the initial brief of allegations or to the additional allegations, or during the preliminary hearing, the parties (and occasionally the court, when this is deemed necessary) must state whether they wish their expert or the one proposed by the opposing party or the one appointed by the court to appear in the trial and the purpose of having him or her appear is (1) to expand on the report; (2) to answer questions; (3) to be cross-examined by the opposing party, and (4) to challenge the other party's expert witness report.

Expert witnesses, together with regular witnesses, parties' declarations and judicial recognition, will normally be examined at trial.

IV RECENT CASE LAW

In its judgment of 8 April 2016, the Spanish Supreme Court, hearing a claim for damages by a victims' association, loss of assets and moral damages in the 2012 Costa Concordia cruise accident, confirmed the legitimacy of the application by analogy of the compensation schedules set out in Law 35/2015 to cases other than motor vehicle accidents. As a result, the €60,000 per person for moral damages that the association was claiming was reduced to €12,000 per person.

UNITED KINGDOM

Clare Connellan¹

I OVERVIEW

Under English law, the basic principle for breach of contract is that a party is entitled to be put in the same position as they would have been had they not sustained the wrong.² As the name suggests, compensatory damages are intended to compensate a claimant for losses suffered as a result of the other party's (wrongful) conduct.

While the concept of compensatory damages is common to several jurisdictions, a distinctive feature of English law is the emphasis on mitigation of loss. The claimant is expected to take all reasonable steps to minimise its loss resulting from the defendant's breach of its obligations. Loss that could have been avoided through reasonable action or inaction by the claimant will not be recoverable. By corollary, if the injured party takes reasonable steps to minimise the loss incurred, the cost of these steps is recoverable and the damages owed by the defendant are reduced by the amount of reduction of loss.³

There are three main categories of recoverable damages under English law: (1) expectation damages; (2) performance damages; and (3) reliance or 'wasted expenditures' damages. Other categories of damages include moral damages, punitive or exemplary damages and non-monetary damages such as specific performance,⁴ but this chapter's focus is on compensatory damages.

Expectation damages are awarded to put the claimant in the position it would have been in but for the breach. The ability of a claimant to recover lost profits will depend on the subject of the breach.⁵ There two types of 'expectation damages' – normal or direct damages (also known as general damages), and consequential damages (also known as special damages).⁶ Normal or general damages follow as a natural and probable consequence of a

1 Clare Connellan is a partner at White & Case LLP. The author thanks Pavini Emiko Singh and Theresa Puthumana, associates at White & Case LLP, for their contributions to this chapter.

2 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 2-002, citing *Livingstone v. Rawyards Coal Co* [1880] 5 App Cas. 25 at 39.

3 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 9-002–9-006.

4 *Chitty on Contracts*, 32nd ed., 2015, Chapter 26, Sections 26-022 – 26-030, 26-044–26-045, and Chapter 27, 27-001–27-004.

5 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Sections 4-0018–19. See also the series of cases concerned with breach of restrictive covenants and damages to account for profits, e.g., *Wrotham Park Estate Co. v. Parkside Homes Ltd* [1974] 1 WLR 798, giving rise to *Wrotham Park* damages.

6 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Sections 3-001–3-016.

breach,⁷ whereas consequential damages are those that do not flow directly from the breach and are particular to the injured party and can therefore be difficult to calculate in financial terms.⁸

Performance damages compensate the cost of curing the defective performance⁹ and 'wasted expenditures' or 'reliance damages' compensate the losses or expenditures incurred by the claimant in reliance on the contract.¹⁰ These damages are aimed at putting the claimant in as good a position as he or she was prior to the promise.¹¹

II QUANTIFICATION OF FINANCIAL LOSS

In English law, the purpose of an award of damages for breach of contract is to compensate the injured party for loss, rather than to punish the wrongdoer. The general rule is that damages should (so far as a monetary award can) place the claimant in the same position as if the contract had been performed.¹² Therefore, damages are usually measured by the difference in value between the contemplated and actual performance of the contract.¹³

To establish entitlement to damages, the claimant is also required to show that adequate steps have been taken to mitigate the damage resulting from the defendant's actions. Failure to take mitigating steps will likely result in the claimant's entitlement to damages being reduced.

In addition to mitigating factors, damages awarded under English law are also influenced by methods of calculation, application discount and interest rates and income tax or capital gains tax.

i Evidence

If a claimant has suffered a loss,¹⁴ there are four key elements that are relevant to establishing a party's entitlement to damages and determining the amount of damages to be awarded: (1) the existence of a wrong; (2) reasonable foreseeability; (3) failure to mitigate the impact of the breach; and (4) chain of causation.

The first and most basic requirement is that in order to establish an entitlement to damages one must prove the existence of a 'wrong'¹⁵ – that is, a breach of contract. Second, a

7 For the position under English law, see *Halsbury's Laws of England*, Section 317, citing *Ratcliff v. Evans* [1892] 2 QB 524 at 528, CA, per Bowen LJ.

8 For the position under English law, see *Halsbury's Laws of England*, Volume 29, Section 317 and H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 3-008.

9 J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Sections 26-020–26-021.

10 *Halsbury's Laws of England*, Volume 29, Section 503.

11 J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Sections 26-020–26-021.

12 *Robinson v. Harman* (1848) 1 Ex 850.

13 H. Wöss and others, *Damages in International Arbitration under Complex Long-Term Contracts* (Oxford University Press, Oxford 2014) para. 4.38. See, e.g., *Durham Tees Valley Airport Ltd v. Bmibaby Ltd* [2010] EWCA Civ 485.

14 Where a loss has been suffered by another party, this can give rise to the so-called 'black hole' problem, where the damages risk falling into a black hole. The English courts have indicated a willingness to find a solution in such circumstances, where appropriate. See, e.g., *McAlpine v. Panatown*, [2001] 1 AC 518.

15 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 1-001.

claimant must establish that the damage is not too remote and that the losses were reasonably foreseeable at the time the parties entered into the contract.¹⁶ The test of reasonable foreseeability was first outlined in *Hadley v. Baxendale* as:

*Where two parties have made a contract, which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e. according to the usual course of things, from such breach of contract itself, or such as 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.*¹⁷

For loss to have been foreseen, it must have been contemplated by the parties and ‘not unlikely’¹⁸ at the date of entering into the contract. Loss is said to have been in contemplation of the parties (and therefore assumed)¹⁹ if, objectively assessed, it could be said to occur in the ordinary course of events, or, if subjectively assessed, there are special circumstances or knowledge attributable to the parties.²⁰

Third, any damages awarded are subject to deductions for any failure to mitigate (or contributory negligence in the case of breaches of duty of care). The defendant carries the burden of proof in relation to establishing the claimant’s actions (or lack thereof) to mitigate damage as a result of the defendant’s breach.²¹ Provided the steps taken by the claimant to minimise the loss incurred are reasonable, the cost of such steps is recoverable even if the steps taken have increased the loss.²² However, any profit accrued as a result of the claimant’s mitigating actions is also credited to the defendant if causation is established, with the latter having the burden of proving the existence and amount of such profit.²³

Fourth, any damages awarded are also subject to any breaks in the chain of causation.²⁴ Irrespective of factual causation, English law can treat some losses as not having been legally caused by the breach, on the basis that it is not fair to hold the defendant responsible for them

16 Wagon Mound (No. 1) [1961] AC 388; J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Sections 26-111 and 26-116. The notion of foreseeability is further analysed below.

17 *Hadley v. Baxendale* (1854) 9 Exch. 341.

18 *Hadley v. Baxendale* (1854) 9 Exch. 341.; [*H. Parsons (Livestock) Ltd v. Uttley Ingham & Co Ltd* [1977] EWCA Civ 13.

19 *Transfield Shipping Inc v. Mercator Shipping Inc (The Achilles)* [2008] UKHL 48; *Supershield Ltd v. Siemens Building Technologies FE Ltd* [2010] EWCA Civ 7; *Rubenstein v. HSBC Bank plc* [2012] EWCA Civ 1184.

20 *Victoria Laundry (Windsor) Ltd v. Newman Industries Ltd* [1949] 2 KB 528.

21 *Lombard North Central plc v. Automobile World (UK) Ltd* [2010] EWCA Civ 20. A claimant should nevertheless consider whether to take steps to show how it has mitigated its loss, as failure to do so can be risky. *Bulkhaul Ltd v. Rhodia Organique Fine Ltd* [2008] EWCA Civ 1452.

22 *Lagden v. O'Connor* [2004] 1 AC 1067, per Lord Scott, at para. 78.

23 *Thai Airways International Public Co Ltd v. KI Holdings Co Ltd (formerly Koito Industries Ltd)* [2015] EWHC 1250 (Comm). See also *Globalia Business Travel SAU (formerly TravelPlan S.A.U) of Spain v. Fulton Shipping Inc of Panama* [2017] UKSC 43, in which the Supreme Court confirmed that the issue turns on causation: where the claimant has obtained a benefit following a breach of contract and this benefit was caused either by the breach or by the claimant’s act of mitigation, the recoverable loss will be reduced by the benefit.

24 C. T. Salomon, ‘Chapter 10: Damages in International Arbitration’, in J. Fellas and J. H. Carter (eds), *International Commercial Arbitration in New York* (2nd ed. Oxford University Press, Oxford 2016), p. 353.

due to a 'break in the chain' or *novus actus interveniens*.²⁵ If the breach of contract was the 'effective' or 'dominant' cause of the loss, damages may be recoverable even if the breach was not the sole cause of the loss.²⁶ Where there are competing causes, a balance of probabilities test applies.²⁷

ii Date of assessment

Under English law, damages are normally assessed at the date of breach of contract unless to do so would not be in the interests of justice.²⁸

However, the date of breach may not be appropriate as the starting point for calculation of damages. For example, a claimant's steps to mitigate the loss may impact the evaluation of the damages. Similarly, where the claimant has not in fact suffered any loss at the date that the actual breach occurred, but only began to suffer loss subsequently, the latter date may be the more appropriate starting point for calculation.

iii Financial projections

Under English law, a claimant must prove the fact of loss and the amount of the loss on the balance of probabilities, that is, 'If the evidence shows a balance in favour of it having happened, then it is proved that it did in fact happen.'²⁹ However, different principles apply for future or projected loss.

Where it is difficult to prove the amount of loss with certainty, the wrongdoer should not be relieved of his or her responsibility to pay.³⁰ Damages can be recovered for 'loss of a chance'. However, this is an inherently uncertain head of loss, and can raise difficult issues of causation and quantification.³¹

The doctrine of 'loss of chance' was introduced in English law by the decision in *Chaplin v. Hicks*,³² but has since evolved considerably. In *Mallett v. McMonagle*, Lord Diplock opined:

*Anything that is more probably than not [the court] treats as certain. But in assessing damages which depend on its view as to what will happen in the future or would have happened in the future if something had not happened in the past, the court must make an estimate as to what are the changes that a particular thing will or would have happened and reflect those chances, whether they are more or less than even, in the amount of damages it awards.*³³

25 See, e.g., *Corr v. IBC Vehicles Ltd* [2008] 1 AC 884, per Lord Bingham at para. 15: 'The rationale of the principle that a *novus actus interveniens* breaks the chain of causation is fairness.'

26 *Galoo v. Bright Grahame Murray* [1994] 1 W.L.R. 1360, at 1374–1375. See also J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Section 26-068: 'If a breach of contract is one of two causes, both co-operating and both of equal efficacy in causing loss to the claimant... the contract-breaker is liable so long as his breach was 'an' effective cause of his loss: the court need not choose which cause was the more effective.'

27 *Nulty and others v. Milton Keynes Borough Council* [2013] EWCA Civ 15, at para. 35: '[T]he court must be satisfied on rational and objective grounds that the case for believing that the suggested means of causation occurred is stronger than the case for not so believing.'

28 *Johnson v. Agnew* [1980] AC 367, per Lord Wilberforce at 401.

29 *Davies v. Taylor* [1974] AC 207 at 213.

30 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Sections 10-001–10-002.

31 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Sections 10-005–10-006. [1911] 2 K.B. 786.

32 *Mallett v. McMonagle* [1970] A.C. 166 at 176.

Establishing a loss of chance requires that there be both a real and a substantial chance – a chance that is negligible is not likely to support recovery of projected damages.³⁴ Similarly, a chance to which only a speculative money value can be assigned is unlikely to succeed.³⁵ However, where the realisation of a chance appears to be virtually certain, the court will consider it appropriate to award what would have been awarded against the defendant originally.³⁶

iv Liquidated damages and penalties

Parties to a contract can agree between them the amount of damages payable for any breaches (stipulating different sums for different breaches).³⁷ The long-standing common law rule is that a term in a contract, which constitutes a penalty, is unenforceable. Therefore, the court will have to determine whether the payment stipulated is a liquidated damage or a penalty. A penalty is a payment of money stipulated as *in terrorem* of the offending party and the liquidated damages are a genuine pre-estimate of damage.³⁸ The Supreme Court in the 2016 conjoined appeals in *Cavendish Square Holdings v. Makdessi* and *ParkingEye Ltd v. Beavis*³⁹ revisited and reinstated the above law on penalties and liquidated damages.

The Court held that the penalties doctrine is applicable only when there is a breach of contract and no matter how extreme a party is penalised, it will amount to a penalty only when it is a result of breach. The courts have no power to regulate parties' primary obligations and the rule is applicable only in the case of secondary obligations. In this judgment, Lords Neuberger and Sumption stated that 'the true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation'.⁴⁰ The Court further observed that whether a clause operates as a primary obligation or secondary obligation is a question of substance and not form.⁴¹

v Discount rates

The calculation of compensatory damages often involves the determination of future losses or 'loss of chance'. When calculating future losses, the application of an appropriate discount rate is required to estimate the expected rate of return had the loss not occurred.

In a consultation by the Ministry of Justice in relation to the Damages Act 1996, the overriding aim behind discount rates was described as to set the rate as accurately as possible so that under-compensation or over-compensation by reason of the accelerated payment of the future losses is avoided as far as possible.⁴²

While this principle was articulated in the specific context of personal injury claims, the general presumption is helpful when considering the general application of discount rates

34 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 10-051.

35 *Halifax Building Society v. Urquhart-Dykes and Lord* [1997] R.P.C. 55 at 87, line 18.

36 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 10-094, referring to *inter alia*, *McGrath v. Kiely and Powell* [1965] I.R. 497 and *White v. Jones*, [1995] 2 A.C. 207 CA.

37 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 16-001.

38 *Dunlop Pneumatic Tyre Co Ltd v. New Garage and Motor Co Ltd* [1915] AC 79.

39 [2016] A.C. 1172.

40 [2016] A.C. 1172 at [32].

41 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 16-014.

42 Ministry of Justice Consultation Paper CP 3/2013, 'Damages Act 1996: The Discount Rate', at p. 4.

to the calculation of compensatory damages. In the discounted cash flow analysis (discussed further below), if a breach of contract results in loss of profits over time, a discount rate is applied to estimate the current value of the cash flow. The discount rate in such instances would typically depend on the asset being valued. For example, while valuing equity, the relevant discount rate would be that most appropriately reflecting the cost of the equity. Discount rates are influenced by a variety of factors including political changes, future inflation, currency devaluation and fluctuating interest rates.

Experts use a variety of discount rate calculation methods when valuing assets including, for example, the capital asset pricing model (which considers a stock's rate of return, the market's rate of return and a risk-free rate) and the weighted average cost of capital (which is usually used to assess a company's value as a whole by estimating the weighted average of new debt and equity needed to operate the company).

vi Currency conversion

The currency contemplated by the contract generally determines the currency for damages to be awarded.⁴³ Where the contract does not provide for a specific currency for the awarding of damages, the damages will be awarded in the currency in which the claimant suffered the loss.⁴⁴

In *Miliangos Respondent v. George Frank (Textiles) Ltd*,⁴⁵ the House of Lords found that the English courts had the authority to give judgment in foreign currency where under a contract, payment obligations are in a foreign currency and the proper law is that of the foreign country, with payment to be made outside the United Kingdom.⁴⁶ The courts will take into account commercial considerations and give judgments in foreign currency or its sterling equivalent at the date when the court authorises the claimant to enforce the judgment.⁴⁷ This protects the claimants against any decrease in the external value of sterling in relation to their own currency, save for in instances where the value of sterling is rising.⁴⁸

The courts have also considered the issue of whether a court has the power to make a cost award to compensate for any exchange rate losses incurred in paying costs. In *Elkamet Kunststofftechnik GmbH v. Saint-Gobain Glass France SA*,⁴⁹ the court held that 'order for costs is designed to compensate the successful party for its expenditure so that exchange rate losses can be compensated in the same way as it is entitled to be compensated by way of interest for being kept out of the money'.⁵⁰

43 *Federal Commerce and Navigation Co Ltd v. Tradax Export SA* [1977] 1 QB 324; J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Section 30-378.

44 *Attorney General of Ghana v. Texaco Overseas Tankships Ltd (The Texaco Melbourne)* [1994] 1 Lloyd's Rep. 473 (HL). See also, *Milan Nigeria Ltd v. Angeliki B Maritime Company* [2011] EWHC 892 (Comm) para 57.

45 [1975] 3 W.L.R. 758.

46 *Miliangos v. George Frank (Textiles) (No. 2)* [1977] Q.B. 489, 497; *Helmsing Schiffahrts v. Malta Drydocks Corp* [1977] 2 Lloyd's Rep. 444, 449.

47 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 20-029.

48 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 20-053.

49 [2016] EWHC 3421 (Pat).

50 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 20-054.

vii Interest on damages

The court has the authority to grant award interest on damages for any period between the date when the cause of action arose and the date of judgment.⁵¹ If the claimant caused unwarrantable delay, interest on damages for such period will be reduced accordingly. A damages claim (including a claim for interest) should therefore be clearly particularised and supported by the necessary written and oral evidence required to prove the claimant's case.

The court has the discretion to award interest at different rates in respect of different periods; in contractual claims, the interest rate should reflect the current commercial rate. The Commercial Court and the Court of Appeal generally award 1 per cent above the base rate. However, if such calculation would put either party in an unfair position (smaller business pays higher interest rate, etc.), the court can adopt an appropriate interest rate to suit the parties.⁵²

Where the damages are calculated in a foreign currency, the commercial borrowing rate in the foreign currency in the relevant country is considered as the relevant interest rate.⁵³

viii Costs

As a general principle, legal costs incurred as a result of breach of contract can be recovered as damages, where they were incurred in actions against third parties or previous actions against the defendant. The costs of the dispute over the breach of contract itself, although caused by the breach usually cannot be claimed as damages as they fall within the exclusive jurisdiction of the courts' costs regime.⁵⁴

As a result of the mitigation principle, legal costs recoverable as contract damages are assessed in the same way as 'indemnity basis' of costs. That is, 'unreasonable' costs are not recoverable under common law principles, nor is proportionality always taken into account.⁵⁵

ix Tax

There are two types of taxation that may apply in relation to an award for damages: (1) income tax; and (2) capital gains tax.

Prior to 1956, the English courts did not reduce awards of damages to account for income tax. However, in *British Transport Commission v. Gourley*, the House of Lords ruled that when calculating damages for personal injuries resulting from a tort, the court will take into account the tax liability in respect of his loss of earnings (both past and prospective).⁵⁶ This rule has been modified over the years in instances where the damages sought would have been taxed.⁵⁷

51 Section 35A of the Senior Courts Act 1981.

52 J. Chitty, H. Beale, *Chitty on Contracts* (32nd ed. Sweet & Maxwell, London 2015), Section 26-240.

53 *Miliangos v. George Frank (Textiles) (No. 2)* [1977] Q.B. 489, 497; *Helmsing Schiffahrts v. Malta Drydocks Corp* [1977] 2 Lloyd's Rep. 444, 449.

54 *Hutchinson v. Harris* [1978] 10 BLR 19.

55 *National Westminster Bank plc v. Rabobank Nederland* [2007] EWHC 1742 (Comm). See also, *Hawksford Trustees Jersey Ltd v. Halliwells LLP (In liquidation)* [2015] EWHC 2996 (Ch).

56 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 18-002, citing *British Transport Commission v. Gourley* [1956] A.C. 185.

57 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 18-005. See e.g., *BskyB Ltd v. HP Enterprise Services UK Ltd*, [2010] EWHC 862 (TCC) at [77], and *Taylor v. O'Connor* [1971] A.C. 115.

Capital gains tax differs from income tax in that it does not cause damages to be reduced. However, the impact of capital gains tax would need to be considered on a case-by-case basis where the application of capital gains tax affects the value of the asset that is said to have suffered the loss.

III EXPERT EVIDENCE

The Civil Procedural Rules 1998 as amended (the Rules) and accompanying Practice Directions deal extensively with the appointment of experts and assessors. At a primary level, the aim of these Rules and Practice Directions is to regulate the use of expert evidence in civil proceedings, in particular to address concerns relating to independence of experts, excessive expenditure and increasing complexity.

i The role of expert evidence in calculation of damages

Experts can play an important role in assessing damages, particularly where damages are influenced by a range of factors occurring both at and after the date of breach or the application of rates of interest are in dispute.

For example, in *Vasiliou v. Hajigeorgiou*⁵⁸ the trial judge found the claimant to be an accomplished restaurateur whose restaurant would have been successful and assessed his loss of profits on that basis. The expected turnover, together with gross and net profit, was calculated with expert evidence and the ultimate decision not to apply a discount was upheld by the Court of Appeal.⁵⁹

ii The court's role excluding and managing expert evidence

English law provides that expert evidence shall be restricted to that which is reasonably required to resolve the proceedings. The court may therefore control the evidence by giving directions in relation to the issues on which it requires evidence, the nature of the evidence required and the way in which the evidence is to be placed before the court.⁶⁰ For instance, in *Dudding v. Royal Bank of Scotland Plc*,⁶¹ the court held that the claimants were entitled to rely on the expert evidence concerning the sale of derivatives by the defendant banks as the evidence was reasonably required in order to resolve the issues.

Courts are required to seek to restrict the excessive or inappropriate use of expert evidence. Under English law, parties are required to seek the court's permission prior to filing an expert report, and their application for permission must include an estimate of the costs of the proposed expert evidence. In *British Airways plc v. Spencer*, the court held that when assessing whether to admit expert evidence, the court will consider whether the evidence is necessary (i.e., whether a decision could be made without it) or if it is of marginal relevance. The courts will strike a balance if it is of marginal relevance by taking into account the value of the claim, the effect of a judgment on the parties, how the commissioning of the evidence would be paid for, and any delay likely to be entailed by the production of such evidence.⁶²

58 [2010] EWCA Civ 1475 CA.

59 H. McGregor, *McGregor on Damages* (20th ed. Sweet & Maxwell, London 2017), Section 10-038; *Vasiliou v. Hajigeorgiou* [2010] EWCA Civ 1475 CA, para. 15.

60 CPR 35.1 and White Book commentary para. 35.1.1 at page 1127.

61 [2017] EWHC 2207 (Ch).

62 [2015] EWHC 2477 (Ch).

Permission given by the court is limited to the expert or field specifically identified in the parties' application, and the court can limit the amount of the expert's fees and expenses that can be recovered from the other party.⁶³ In *Darby Properties Ltd and Darby Investments Ltd v. Lloyds Bank plc*,⁶⁴ the Master reviewed several authorities on expert evidence in interest rate swap cases together with case law. On finding that there was not a consistent approach, he concluded that while a judge would benefit from evidence explaining the specific financial products, this could be done by way of factual evidence and therefore expert evidence was not required.⁶⁵

Judges are required to give reasons for preferring the evidence of one expert over another and failure to provide such reasoning may be considered valid grounds for appeal.⁶⁶

iii Independence of experts

English law provides that experts must provide opinions that are independent and uninfluenced by the pressures of litigation. Experts are required to assist the court by providing objective, unbiased opinions on matters within their expertise by considering all material facts (including those that might detract from their opinions) and should avoid assuming the role of an advocate. If a question or issue falls outside their expertise or they are unable to reach a definite opinion, they should make this clear to the court and any change of view should be communicated to all the parties without any delay (and when appropriate, to the court).⁶⁷ In the case of *Arroyo and others v. Equion Energia Ltd* (formerly known as BP Exploration Co (Colombia) Ltd),⁶⁸ the court held that the 'deliberate and serious breach' of the expert was highly relevant in the court's assessment of order of costs paid on an indemnity basis. Similarly, in the case of *Igloo Regeneration (General Partner) Ltd v. Powell Williams Partnership*,⁶⁹ a partial indemnity costs award was made against the claimant related to the conduct of its inexperienced expert engineer who made concessions in his joint statement, which undermined the claimant's case on liability.

The courts have reiterated the importance of experts' independence and impartiality including in recent cases including *Watts v. The Secretary of the State for Health and Bank of Ireland v. Watts Group*.⁷⁰ In the former, the court went so far as to criticise the expert for choosing to 'ignore or play down matters that were inconvenient to her assessment of the case'.⁷¹

iv Novel science and methods

Expert evidence is typically helpful in the calculation of damages under two methods: (1) the discounted cash flow method; and (2) comparable transactions and comparable trading multiples method.

63 CPR 35.4.

64 [2016] EWHC 2494 (Ch), See also, *Barings Plc (In Liquidation) v. Coopers & Lybrand* (No. 2) [2001] Lloyd's Rep. Bank. 85.

65 See also White Book commentary para. 35.1.1 at page 1127.

66 *Flannery and another v. Halifax Estate Agencies Ltd* [2000] 1 W.L.R. 377.

67 CPR 35 paras. 2.1-2.5 and White Book commentary para. 35.18 at page 1160.

68 [2016] EWHC 3348 (TCC).

69 [2013] EWHC 1718 (TCC).

70 *Bank of Ireland and another v. Watts Group Plc* [2017] EWHC 1667 (TCC).

71 *Watts v. The Secretary of State for Health* [2016] EWHC 2835 (QB) at para. 64.

The discounted cash flow method projects future cash flows and uses a discount rate to estimate the current value of the projected cash flows. This method is best used in instances where the parties are trying to calculate the earning potential of an asset in the future and require expert evidence in the accurate forecasting of such cash flows. Among other things, expert evidence is used to determine the time period in the future that should be used to assess the cash flows, and the appropriate discount rates to be applied in the calculation of the asset value. As explained above, discount rates such as capital asset pricing model and weighted average cost of capital are two such methods.

Comparable transactions or comparable trading multiples primarily use publicly reported transactions and share prices to arrive at an estimated value of the asset in question, provided that sufficiently comparable transactions and prices exist in the market. Expert evidence can be crucial in determining the comparability of prices in the public domain, and the relevance of the proposed comparisons.

The EU General Data Protection Regulation ((EU) 2016/679) (GDPR) is in effect as of 25 May 2018. The Regulation is aimed at addressing the collection of data and the way it is processed and used by both individuals and organisations, including in the communication and sharing of information. The full impact of the GDPR on evidence in litigation or arbitration remains to be seen.

IV RECENT CASE LAW

i **Axa Insurance UK Plc v. Financial Claims Solutions Ltd [2018] EWCA Civ 1330**

The defendants committed serious frauds by issuing two sets of fictitious personal injury claims based on fake documents to the insurance companies. The claimant insurance company conducted an investigation, discovered the claimant's fraudulent conduct, and brought claims against the defendants seeking both compensatory and exemplary damages. The lower court awarded compensatory damages, but rejected their claim for exemplary damages stating that the fraud was discovered before the defendants made any profits and, therefore, the second category of *Rookes v. Barnard*⁷² did not apply.

On appeal, the court held that the lower court wrongly applied the *Rookes* case. The court explained that the second category of *Rookes* applies to cases where 'the defendant's conduct has been calculated to make a profit for himself which may well exceed the compensation payable to the claimant'.⁷³ In the present case, the compensatory damages granted were limited to the cost of investigation, which was a much lesser sum compared to the profit the defendants would have made had the fraud been successfully executed. The court observed that exemplary damages are 'available for the case where compensatory damages are inadequate to remove the wrongful gain achieved by the tort'⁷⁴ and they are punitive in nature.⁷⁵ The court further observed, 'the second category requires the Court to

72 (No. 1) [1964] A.C. 1129, at para. 1226: 'Cases in the second category are those in which the defendant's conduct has been calculated by him to make a profit for himself which may well exceed the compensation payable to the plaintiff.'

73 *Axa Insurance UK Plc v. Financial Claims Solutions Ltd* [2018] EWCA Civ 1330, at paras. 15 and 25.

74 *Axa Insurance UK Plc v. Financial Claims Solutions Ltd* [2018] EWCA Civ 1330, at para. 19.

75 *Axa Insurance UK Plc v. Financial Claims Solutions Ltd* [2018] EWCA Civ 1330, paras 35; *Ramzan v. Brookwide Ltd* [2011] EWCA Civ 985, [2012] 1 All E.R. 903. Exemplary damages should be principled and proportionate, and the principled basis is to make a punitive award.

analyse the position prospectively when the tort is committed, at which time the tortfeasor may or may not ultimately achieve the profit it seeks to achieve'.⁷⁶ Given the seriousness of the claim and the need to deter and punish the outrageous conduct and abusive behaviour, the court awarded exemplary damages.⁷⁷

ii One Step (Support) Ltd v. Morris-Garner [2018] UKSC 20

The appellant employees acted in breach of their restrictive covenants in their employment contracts. The employer claimant chose to claim 'negotiation damages' under the principles of *Wrotham Park Estate Co Ltd v. Parkside Homes Ltd*.⁷⁸ One of the reasons given by the appellant for seeking negotiation damages was the difficulty in establishing the loss the business suffered as a result of the employees' conduct. The lower courts applied the *Wrotham Park* principle and granted the employer negotiation damages; the defendants appealed. Allowing the appeal, the court held that the lower court wrongly applied the *Wrotham Park* principle, and provided clarification on the correct application of the *Wrotham Park* principle and granting 'negotiation damages'.

The court observed that the hypothetical fees that the parties would have agreed for release of contractual damages for breach of contract under the *Wrotham Park* principle was not compensatory damages. It clarified that common law damages for breach of contract is not a matter of discretion for the judge; it is claimed as of right, and awarded on the basis of legal principles.⁷⁹ The courts are not justified in granting negotiation damages just because it was difficult to quantify the financial loss and negotiation damages was considered to be a just response. Accepting that financial loss in the present case scenario was difficult to quantify, the court held that it was still a 'familiar type of loss for which damages were frequently awarded and could be quantified in a conventional manner. Therefore, the hypothetical release fee is not itself the measure of the claimant's loss in this case.'⁸⁰

76 *Axa Insurance UK Plc v. Financial Claims Solutions Ltd* [2018] EWCA Civ 1330, at para. 27.

77 *Axa Insurance UK Plc v. Financial Claims Solutions Ltd* [2018] EWCA Civ 1330, at paras. 23 and 34: the possibility of criminal or contempt proceedings against the defendants is irrelevant to the question of whether or not exemplary damages is to be awarded.

78 [1974] 1 W.L.R. 798.

79 *One Step (Support) Ltd v. Morris-Garner* [2018] UKSC 20, at para. 95: '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.... The rationale is that the claimant has in substance been deprived of a valuable asset, and his loss can therefore be measured by determining the economic value of the right in question, considered as an asset. The defendant has taken something for nothing, for which the claimant was entitled to require payment.'

80 *One Step (Support) Ltd v. Morris-Garner* [2018] UKSC 20.

UNITED STATES

*Gary J Mennitt, Ryan M Moore and Nicholas A Passaro*¹

I OVERVIEW

The US legal system is made up of a network of at least 50 different state jurisdictions and a complex federal court system, itself with numerous different jurisdictions. As a result, approaches to compensatory damages will vary from jurisdiction to jurisdiction (and sometimes from court to court). Nevertheless, certain core principles arise across jurisdictions, which apply generally across cases.

Very generally, the goal of compensatory damages is to ‘compensate’ the plaintiff for a legally recognised loss caused by the defendant. Key to that compensation is that although the law will make best efforts to compensate the plaintiff entirely for his or her loss, the plaintiff should not be permitted to recover a windfall. In determining the scope and amount of a proper compensatory damages award, courts take into consideration evidence submitted by the parties, including expert evidence in more complicated cases. And in many cases, if a plaintiff fails to clearly establish a definable injury, his or her cause of action will be dismissed in its entirety.

Other types of damages are available in US courts, such as restitution damages, equitable damages or punitive damages, dependent upon the given case. For the purposes of this chapter we have focused our discussion on general principles of law applied across the United States federal court system regarding compensatory damages. Where we have referenced law or principles arising from other jurisdictions – for example, certain noteworthy principles applied in specific state jurisdictions – we have indicated the distinction.

II QUANTIFICATION OF FINANCIAL LOSS

i Introduction

In the United States, the general goal of compensatory damages is ‘to restore the injured party, to the extent possible, to the position that would have been occupied had the wrong not occurred’.² In aiming to achieve that goal, different sets of circumstances necessitate unique approaches. Calculations often need to be made about the value of property, medical expenses, lost sales and lost wages. Even more complicated are the calculations necessary to compensate a plaintiff for lost future earnings, either as wages for an individual or sales for a business, or for future pain and suffering caused by a tortious injury. These varying types of

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² *In re Methyl Tertiary Butyl Ether (MTBE) Products Liability Litigation*, 643 F. Supp. 2d 446, 455 (S.D.N.Y. 2009).

damages can be demonstrated through a corresponding variety of evidence, with the court system striving to achieve the goal of placing a plaintiff in the position he or she was in or would have been in but for the defendant's wrongful conduct.

ii Evidence

Evidence for proving damages in the United States can come in the form of records, documents and testimony from witnesses and experts.³ The law of evidence is complex but it is worth noting here that in business disputes, most reliable commercial records will be admissible. In some straightforward cases, damages are 'within the common sense of the jury and do not require expert testimony'.⁴ For example, when assessing damages in a breach of contract case, accurate records could prove with reasonable certainty any financial loss resulting from the breach. Additionally, the plaintiff could testify about any expenses that were incurred because of the breach. In more complicated cases, however, experts may be necessary to testify about calculations derived from the evidence or other factors relevant to a damages evaluation, including, for example, relevant industry norms regarding lost wages, complicated financial projections and economics, or the value of damaged or destroyed property. These types of expert testimony evidence will be discussed further in Section III.

iii Date of assessment

The date from which damages are assessed can vary based on the type of case. In a contract case, damages are assessed from the date of breach.⁵ In a tort case, damages are assessed from the date of the incident giving rise to the claim (i.e., the date of the injury). That date-of-injury can often be different from the date of the defendant's conduct giving rise to that injury.⁶ For example, if a defendant is found liable for a danger to his or her property, such as a dangerous hazard at their place of business, the date of assessment would not be when the defendant caused or allowed the hazard to exist, but when the plaintiff was injured by the hazard. These dates could be days, months or even many years apart.

iv Financial projections

Financial projections become relevant when calculating damages that have not yet been incurred, but with reasonable certainty will be incurred in the future as a result of the defendant's conduct. For example, in contract cases, one category of damages can be the future loss of earnings or sales caused by the defendant's breach of contract. Tort cases can also involve damages constituting future loss of earnings or future pain and suffering arising from a defendant's tortious conduct. As previously discussed, these types of prospective damages typically would be demonstrated by expert witnesses who are familiar with typical sales of a business of that size in that industry, typical wage growth of someone of the plaintiff's education and skill level in their industry and geographical location, or relevant medical

3 See *Stearns' Properties v. Trans-World Holding Corp.*, 492 F. Supp. 238, 242–45 (D. Nev. 1980) (discussing evidence for proving damages).

4 See *Cummings v. Standard Register Co.*, 265 F.3d 56, 67 (1st Cir. 2001) (discussing determinations of front pay damages under Massachusetts law).

5 *First Federal Lincoln Bank v. U.S.*, 518 F.3d 1308, 1316 (Fed. Cir. 2008).

6 See *Culver v. Slater Boat Co.*, 722 F.2d 114, 117 (5th Cir. 1983) (calculating damages from the time of injury).

knowledge.⁷ These projections often are necessary to assist a jury in understanding the full scope of a plaintiff's damages in order to put the plaintiff in the position they would have been in but for the defendant's conduct. A significant limitation on projected damages is that they must be grounded in the facts and not speculative.

v Assumptions

Assumptions are rarely made in damages calculations in United States courts, regardless of the specific jurisdiction, because in most circumstances damages must be proven as an essential element of the *prima facie* tort or breach of contract claim. That being said, sometimes assumptions have to be made in certain cases, such as where expert testimony is necessary to calculate future earnings. An example would be that if a plaintiff was physically injured and could no longer work in his or her prior employment, an assumption would be that he or she would have earned as much as someone of his or her education and skill in that area over an average-length career.⁸ This very well may not have been the case, but it is an assumption that courts and experts often make to try to put the plaintiff in the appropriate position as accurately as possible.⁹ Again, such assumptions must be grounded in statistics and reliable evidence and not speculative.

vi Discount rates

In cases involving future economic damages such as lost wages or profits, where the award will be given in a lump sum, calculations must discount the amounts to present value. The discount rate is typically some safe form of investment to properly account for the added time value of the award.¹⁰ For example, if a business proves it lost future profits over 10 years, its award will be worth its present value, plus its investment over 10 years in a low-risk income-producing bond, bank account or similar vehicle. Since the profits would have come slowly over those 10 years, the lump sum award would need to be discounted by the likely investment returns the plaintiff will (or could) make if awarded the entire lump sum immediately. This all follows from the goal of putting the plaintiff in the position he or she would have been in but for the defendant's conduct – no better, no worse.

vii Currency conversion

Courts in the United States generally award judgments in US dollars and ignore fluctuations in the value of the dollar over the course of time from the injury until the judgment. When

7 See *Energy Capital Corp. v. U.S.*, 302 F.3d 1314, 1330–34 (Fed. Cir. 2002) (discussing expert testimony in calculating loss of future profits); *Jones & Laughlin Steel Corp. v. Pfeifer*, 462 U.S. 523, 533 (1983) (discussing assumptions in calculating loss of future wages); *Norcia v. Dieber's Castle Tavern, Ltd.*, 980 F. Supp. 2d 492, 505 (S.D.N.Y. 2013) (discussing the use of actuarial tables to project life span in calculating compensation for pain and suffering under New York law).

8 See *Jones & Laughlin Steel Corp. v. Pfeifer*, 462 U.S. 523, 533 (1983) (noting that '[i]n calculating damages, it is assumed that if the injured party had not been disabled, he would have continued to work, and to receive wages at periodic intervals until retirement' (emphasis added)).

9 See *id.* at 533–34. ('The lost [wage] stream's length cannot be known with certainty.... Given the complexity of trying to make an exact calculation, litigants frequently follow the relatively simple course of assuming that the worker would have continued to work up until a specific date certain. In this case, for example, both parties agreed that the petitioner would have continued to work until age 65 (12.5 more years) if he had not been injured.')

10 Dunn, R.L. & Harry, E.P., 'Modeling and Discounting Future Damages', *Journal of Accountancy* (2002).

plaintiffs allege damages in a foreign currency, many jurisdictions (20 states) have adopted the provisions of the Uniform Foreign-Money Claims Act. For example, Chapter 2337 of the Ohio Revised Code details the definitions under the Uniform Foreign-Money Claims Act, as well as when it is to be applied.¹¹ The Act provides that awards given in foreign currency will be converted at a bank-offered rate on the day the award is paid to the plaintiff or to the official designated to enforce the judgment.¹²

viii Interest on damages

Pre-judgment and post-judgment interest on damages can vary greatly based on the cause of action and the forum. For example, under the Civil Rights Act of 1964, interest on backpay is statutorily excluded from being awarded.¹³ But under common law, pre-judgment interest was generally only allowed for liquidated damages or damages that were ‘relatively certain and ascertainable by reference to established market values’.¹⁴ Different local jurisdictions are also able to implement specific rules; for example, in the state of Pennsylvania, interest is not allowed to be a part of a damages award for personal injuries.¹⁵ In New York, pre- and post-judgment interest is awarded as-of-right in many cases.¹⁶

ix Costs

Costs, or out-of-pocket damages, may be awarded along with other compensatory damages in certain circumstances. In breach of contract cases, awardable costs might include expenditure the plaintiff made in reliance on the defendant’s agreement under the contract.¹⁷ In tort cases, awardable costs might be expenditure the plaintiff had to make as a result of the defendant’s tortious conduct, such as the costs of medical bills or for replacing damaged or destroyed property. Costs might be discounted by mitigation principles, but they are awarded nevertheless. However, under the so-called ‘American Rule’, attorneys’ fees are generally not awarded to the prevailing party in litigation absent an express statutory or contractual fee-shifting provision. This is a major distinction from many other jurisdictions.

x Tax

In the United States, compensatory damages awarded for physical injury or physical sickness are not included as taxable income.¹⁸ Purely economic damages or those stemming from claims involving emotional distress, however, are included as ordinary taxable income.¹⁹ Additionally, interest on any award, awards for lost wages or profits, awards for emotional

11 23 Ohio Rev. Code § 2337.

12 Uniform Foreign Money-Judgments Claims Act, 13 U.L.A. 23 (1989).

13 42 U.S.C. § 1981a(b)(2) (‘Compensatory damages awarded under this section shall not include backpay, interest on backpay...’).

14 See *General Motors Corp. v. Devex Corp.*, 461 U.S. 648, 652 n.5 (1983); *Rau v. Apple-Rio Management Co.*, 85 F. Supp. 2d 1344, 1349 (N.D. Ga. 1999), *aff’d*, 251 F.3d 161 (11th Cir. 2001).

15 *W.D. Rubright Co. v. International Harvester Co.*, 358 F. Supp. 1388, 1394 (W.D. Pa. 1973).

16 N.Y. C.P.L.R. §§ 5001, 5002 (2018).

17 See *Energy Northwest v. U.S.*, 641 F.3d 1300, 1309 (Fed. Cir. 2011) (noting that ‘[a] plaintiff is entitled to recover costs that were caused by the defendant’s breach... so long as the cumulative result is a reasonable certainty that the awarded costs were actually caused by the breach.’).

18 Publication 525, ‘Taxable and Nontaxable Income’, Internal Revenue Service, p. 19 (2017).

19 *id.*; see *infra* note 54.

distress, and attorney fees and costs are all taxable as ordinary income.²⁰ Generally, the US taxing authorities will ‘look through’ the litigation to determine whether the underlying claim relates to what would ordinarily be taxable income. To take a simple example, an award of lost income is generally taxable because had the income been paid when due it would have been taxable.

III EXPERT EVIDENCE

i Introduction

In United States federal courts,²¹ the admission of expert evidence regarding all matters, including damages, is governed by the Federal Rules of Evidence. Only properly qualified experts may provide evidence on an issue in a case,²² and the rules specifically allow experts to give opinions on ultimate issues in a case, including damages.²³ Very generally, courts act as gatekeepers and allow expert testimony where it is reliable and would assist the trier of fact (including a petit jury) in determining an issue in the case, including the calculation of appropriate damages.

ii The role of expert evidence in the calculation of damages

As discussed above, experts are often called upon in cases to evaluate and give opinions on the damages caused by a defendant’s wrongful conduct. Often, the evaluation of relevant economic, scientific or medical issues is required to project an individual’s lost future earnings, calculate a company’s lost profits, determine the diminished value of a business enterprise, or calculate future pain and suffering attendant to a past injury. Over the last few decades, United States courts have encouraged the presentation of expert testimony on these (and other) issues, principally in an effort to make the job of the fact-finder easier and more dependable.²⁴

iii The court’s role excluding and managing expert evidence

Prior to the introduction of expert evidence, the court must first make threshold determinations on the expert’s qualifications and the relevance of the expert’s testimony to the issues in the case. Federal Rule of Evidence 702, which governs expert testimony, provides:

If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise.

20 id. at 29.

21 Because of the variation of treatment of expert witnesses and their ability to testify as to damages in a given case among United States jurisdictions, we focus our discussion on the rules applicable to cases in United States federal courts. Note, however, that, even within the federal system, treatment may vary across federal courts in different jurisdictions. Nonetheless, as discussed in the introduction, we have framed the discussion around core principles generally uniform across jurisdictions.

22 See Federal Rule of Evidence 702.

23 See Federal Rule of Evidence 704.

24 4 J. Weinstein & M. Berger, *Weinstein’s Federal Evidence* § 703.03[1] (2d ed. 2006) (economics experts may ‘assist the trier of fact to understand the facts already in the record, even if all it does is put those facts into context’).

Interpreting this Rule, a series of cases from the Supreme Court of the United States govern courts' role as 'gatekeepers' to ensure that any and all expert testimony 'is not only relevant, but reliable'.²⁵

The seminal case, *Daubert v. Merrel Dow Pharmaceuticals, Inc.*, articulated a two-prong test to assist trial judges in evaluating the admissibility of expert testimony. Daubert held that, first, '[t]he subject of an expert's testimony must be "scientific knowledge"', which ensures 'evidentiary reliability', explaining:

*[t]he adjective 'scientific' implies a grounding in the methods and procedures of science. Similarly, the word 'knowledge' connotes more than subjective belief or unsupported speculation. The term applies to any body of known facts or to any body of ideas inferred from such facts or accepted as truths on good grounds. Of course, it would be unreasonable to conclude that the subject of scientific testimony must be 'known' to a certainty; arguably, there are no certainties in science. But, in order to qualify as 'scientific knowledge,' an inference or assertion must be derived by the scientific method. Proposed testimony must be supported by appropriate validation – i.e., 'good grounds,' based on what is known.*²⁶

Daubert's second prong requires that the expert evidence or testimony 'assist the trier of fact to understand the evidence or to determine a fact in issue', essentially a relevancy test.²⁷ Expert evidence or testimony that 'does not relate to any issue in the case is not relevant and, ergo, non-helpful'.²⁸

Thus, under *Daubert*, a court faced with a proffer of expert evidence or testimony 'must determine at the outset... whether the expert is proposing to testify to (1) scientific knowledge that (2) will assist the trier of fact to understand or determine a fact in issue'.²⁹ The Supreme Court identified several factors that 'will bear on the inquiry', including whether an expert's methodology 'can be (and has been tested)' or 'subjected to peer review and publication'; 'the known or potential rate of error'; and the 'general acceptance' of the expert's methodology.³⁰ The Supreme Court cautioned, though, that the inquiry is a 'flexible one', focused 'solely on principles and methodology, not on the conclusions that they generate'.³¹

Since *Daubert*, the Supreme Court of the United States has stated clearly, in *Kumho Tire Co. v. Carmichael*,³² that *Daubert's* 'general holding – setting forth the trial judge's "gatekeeping" obligation – applies not only to testimony based on "scientific" knowledge, but also to testimony based on "technical" and "other specialized" knowledge'.³³ This includes expert testimony on damages.

Two cases are demonstrative of how the Daubert standard applies to experts asked to proffer opinions on damages. In *Zenith Electronics Corp. v. WH-TV Broadcasting Corp.*,³⁴ WH-TV, a digital television company based in Puerto Rico, was sued by Zenith Electronics Company to collect unpaid bills for television set-top cable boxes Zenith sold to WH-TV.

25 *Daubert v. Merrel Dow Pharma., Inc.*, 509 U.S. 579, 589 (1993).

26 *id.* at 589–90.

27 *id.* at 591.

28 *id.*

29 *id.* at 592.

30 *id.* at 592–94.

31 *id.* at 594–95.

32 526 U.S. 137 (1999).

33 *Kumho Tire Co.*, 526 U.S. at 141.

34 395 F.3d 416 (7th Cir. 2005) (Easterbrook, J.).

WH-TV filed a counterclaim, seeking to recover lost profits caused by certain alleged defects in the cable boxes it purchased from Zenith. In support of its counterclaim, WH-TV proposed to rely on the testimony of an expert that its business ‘would have grown rapidly, and its profits ballooned’, if Zenith’s boxes has been able to perform as promised.³⁵ On appeal, the federal appellate court affirmed the trial court’s exclusion of the expert’s testimony, finding the expert had failed to gather all the relevant facts and had failed to apply reliable principles and methods. Specifically, the court took issue with the expert’s ‘failure to look outside San Juan, even for a reality check’, in collecting data for his projection; and found the expert’s reliance on his own ‘expertise’, ‘awareness’ and ‘industry expertise’, as opposed to a specific methodology, rendered his testimony unreliable.³⁶ Key to the court’s decision was the recognition that even ‘social science has tools to isolate the effects of multiple variables’.³⁷ Because WH-TV’s expert made no reference to such an ‘empirical toolkit’, his opinion on damages was unreliable and inadmissible at trial.³⁸ In contrast, in *Synergetics, Inc. v. Hurst*,³⁹ another federal appellate court acknowledged that although the relevant methodology for calculating damages may vary, ‘so long as the methods employed [by the expert] are scientifically valid’, the mere disagreement that another method should be used does not warrant exclusion of the expert testimony.⁴⁰ Rather, the proper way to challenge the expert’s assumptions and methodologies is through cross-examination and the opposing party presenting its own expert witness as to damages.⁴¹

iv Independence of experts

Owing to the adversarial nature of the legal process in the United States, experts are chosen, prepared and paid by the litigants whom their opinions support. As a result, a question of the independence of experts (most commonly focused on their financial interest for providing the relevant opinion) is common in most litigation in which an expert opinion is necessary. For example, Judge Posner (a well-respected American jurist) has observed that ‘[m]any experts are willing for a generous (and sometimes for a modest) fee to bend their science in the direction from which their fee is coming’.⁴²

35 *Zenith Elec. Corp.*, 395 F.3d at 417–18.

36 *id.* at 418–19.

37 *id.* at 419.

38 *id.* Note, however, that an opinion based on experience alone is not *per se* disqualifying. In certain fields, experience is the predominant basis for reliable expert testimony, as long as the expert is able to testify as to the methodology used to come to the relevant conclusion. See, e.g., *United States v. Jones*, 107 F.3d 1147 (6th Cir. 1997) (handwriting expert with years of practical experience and extensive training who explained methodology in detail); *Tassin v. Sears Roebuck*, 946 F. Supp. 1241, 1248 (M.D. La. 1996) (engineer’s testimony can be admissible as expert opinion where ‘based on facts, a reasonable investigation, and traditional technical/mechanical expertise’, and the expert ‘provides a reasonable link between the information and procedures he uses and the conclusions he reaches’).

39 477 F.3d 949 (8th Cir. 2007).

40 *Synergetics, Inc.*, 477 F.3d at 956.

41 *id.*

42 *Indianapolis Colts, Inc. v. Metro. Balt. Football Club Ltd. P’ship*, 34 F.3d 410, 415 (7th Cir. 1994).

To address this issue, some scholars and judges have advocated for an increased use of Federal Rule of Evidence 706, which explicitly confers on federal judges the authority to appoint experts on their own.⁴³

v Challenging experts' credentials

Challenges to a party's expert witness are done through motions to disqualify the expert or exclude his or her testimony. Experts must offer opinions only on those issues actually within their expertise.⁴⁴ Mere exposure to an area does not make one a qualified expert, and courts have excluded experts where their testimony did not arise from the experts' true areas of expertise.⁴⁵ That said, standards for qualifying experts are liberal and depend on the relevant field.⁴⁶

vi Novel science and methods

Prior to the *Daubert* decision, the admission of expert evidence regarding novel science and methods was governed by the 'general acceptance' test articulated seventy years prior in *Frye v. United States*.⁴⁷ In determining the admissibility of evidence derived from a 'crude precursor to the polygraph machine',⁴⁸ the *Frye* court explained:

*[j]ust when a scientific principle or discovery crosses the line between the experimental and demonstrable stages is difficult to define. Somewhere in this twilight zone the evidential force of the principle must be recognized, and while courts will go a long way in admitting expert testimony deduced from a well-recognized scientific principle or discovery, the thing from which the deduction is made must be sufficiently established to have gained general acceptance in the particular field in which it belongs.*⁴⁹

In *Frye*, because the technology at issue had 'not yet gained such standing and scientific recognition among physiological and psychological authorities as would justify the courts in admitting expert testimony deduced from the discovery, development, and experiments thus far made', the evidence was excluded.⁵⁰

43 See, e.g., J. Gregory Sidak, Court-Appointed Neutral Economic Experts, 9(2) *J. of Competition Law & Econ* 359 (2013).

44 See, e.g., *Smith v. Hobart Mfg. Co.*, 185 F. Supp. 751, 756 (E.D. Pa. 1960) ('something more than the self-serving statement of the expert should be required to qualify him').

45 See, e.g., *United States v. Kelly*, 6 F. Supp. 2d 1168, 1184 (D. Kan. 1998) (disqualifying expert because, *inter alia*, 'the court's impression is that [the expert's] qualifications are largely a matter provable only through his own opinion of himself'); *Diaz v. Jonson Matthey, Inc.*, 893 F. Supp. 358, 363 (D.N.J. 1995) (excluding expert's testimony where expert was not qualified in relevant subject area and based his 'expertise' on reading articles on the subject matter prior to giving opinion).

46 See, e.g., *Santos v. Posadas de P.R. Assocs., Inc.*, 452 F.3d 59, 63 (1st Cir. 2006).

47 54 App. D.C. 46, 472, 93 F. 1013, 1014 (1923).

48 *Daubert*, 509 U.S. at 585.

49 *Frye*, 54 App. D.C. at 47, 293 F. at 1014.

50 *ibid.*

As recognised in *Daubert, Frye's* 'general acceptance' test for novel science or methods was superseded by the Federal Rules of Evidence governing expert evidence and *Daubert* itself.⁵¹ But many other jurisdictions within the United States still use some version of the *Frye* standard.

vii Oral and written submissions

Expert evidence can be in the form of oral or written submissions to the court. Typically, an expert will submit evidence prior to trial in the form of a written expert opinion. That expert opinion will contain not only the articulation of the substance of the expert's opinion, but also the expert's qualifications to give that opinion and the facts referenced and methodology used to reach the conclusions contained in the expert's substantive opinion. Should the case go to trial, the expert will then give oral testimony before the fact finder, and be subject to cross-examination by counsel for the opposing party.

IV RECENT CASE LAW

i Rieger v. Giant Eagle, Inc

In the United States, punitive damages go beyond mere compensation and are designed to punish the defendant for his or her tortious behaviour, and to discourage similar behaviour by others. The appropriate limiting ratio of punitive to compensatory damages is an area that has received much attention and continues to develop. In 2003, the Supreme Court offered some guidance by stating that '[w]hen compensatory damages are substantial, then a lesser ratio, perhaps only equal to compensatory damages, can reach the outermost limit of the due process guarantee'.⁵² This 1:1 ratio was reiterated by the Supreme Court in the 2008 *State Farm* case.⁵³

However, a recent case suggests that lower courts are declining to follow, or working around, the Supreme Court's guidance. In *Rieger v. Giant Eagle*, an Ohio appellate court resolved a challenge to an Ohio statute that limited punitive damages to a 2:1 ratio.⁵⁴ The case involved a jury award of US\$121,000 in compensatory damages and US\$1,198,000 in punitive damages.⁵⁵ The trial court initially applied the Ohio statute, limiting the award to the 2:1 ratio, and the plaintiff argued the Ohio statute was unconstitutional as applied.⁵⁶ The trial court agreed with the plaintiff, saying that the original award was not excessive and was within the confines of the purpose of punitive damages – to deter and punish.⁵⁷ On appeal, the court overruled that decision, stated that the statute was constitutional and reinstated the modified 2:1 ratio award.⁵⁸

Although the Ohio Court of Appeals cited *State Farm*, the court nonetheless found that the Ohio statute's 2:1 ratio fell within what was permitted.⁵⁹ The lower court had found the

51 *Daubert*, 509 U.S. at 587.

52 *State Farm Mut. Auto. Ins. Co. v. Campbell*, 538 U.S. 408, 425 (2003).

53 *See Exxon Shipping Co. v. Baker*, 554 U.S. 471, 514 (2008).

54 *Rieger v. Giant Eagle, Inc.*, 103 N.E. 3d 851 (Ohio Ct. App. 2018).

55 *id.*

56 *id.* at 855-56.

57 *id.*

58 *id.*

59 *id.* at 859-60.

2:1 ratio too restrictive in ruling it was unconstitutional (per Ohio state constitution), and the Supreme Court's guidance in *State Farm* indicated that the Ohio 2:1 statutory ratio was too high. This area of the law will no doubt continue to develop.

ii The Tax Cuts and Jobs Act

Earlier this year, the United States significantly modified its tax code when Congress passed the Tax Cuts and Jobs Act (the Act). Part of the Act reduced the number of itemised deductions (i.e., certain expenditures that could be used to lower person's taxable income) available to taxpayers, including certain deductions taxpayers could take involving damages awards in litigation.

Since the Supreme Court's decision in *Commissioner of Internal Revenue v. Banks*,⁶⁰ taxpayers are required to pay federal income tax on 100 per cent of all taxable damages awards,⁶¹ regardless of any contingency fees those taxpayers had to pay to their attorneys. Nevertheless, prior to the passage of the Act, taxpayers could take as a miscellaneous deduction the full amount of that contingency fee, essentially rendering that percentage of the damages award non-taxable income.

Under the new law, taxpayers are no longer permitted to take this type of a deduction for contingency or other attorneys' fees in 2018 and beyond.⁶² For example, if an individual is awarded, as compensatory damages, US\$100,000 in taxable damages in an applicable case, and that same individual agreed to a contingency fee with his or her attorney, which granted the attorney 40 per cent of any damages award as compensation, the individual would walk away with US\$60,000 from the damages award after paying his attorney US\$40,000 of that same award. Prior to the Act taking effect, that individual could take a deduction for that US\$40,000 contingency fee, and only pay federal income taxes on the US\$60,000 he or she actually received from the damages award. But under the new Act, the individual likely will have to pay income tax on the full US\$100,000 damages award, regardless of how much of that award he or she was required to pay to his or her attorney.

Note, however, that the Act still is very new, and courts, regulators and businesses around the country are coping with the challenges associated with understanding, implementing and enforcing a major change in the tax code. This particular consequence for those recovering damages represents merely one way in which the law will be impacting plaintiffs in coming years.

60 See *Commissioner of Internal Revenue v. Banks*, 543 U.S. 426 (2005).

61 See *supra* at note 18, p. 19; 29 for discussion of taxable versus non-taxable damages awards.

62 Tax Cuts and Jobs Act, Pub. L. No. 115-97, Sec. 11045 (2017).

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He practises in the field of licensing, distribution and franchise disputes, and they span different industries ranging from computer software to boiler technology to pharmaceutical products. William has a special interest in the field of assessment of damages and valuation methodology, as he believes that most disputes would be ultimately concerned with damages and its assessment – he is familiar with the technical and legal aspects of this area, which is valued by clients.

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