Singapore Journal of Legal Studies
[2023] 283–304

TOWARDS A RECONSTRUCTION OF THE RULE AGAINST PENALTIES USING THE 'JUST COMPENSATION' CRITERION

Moshood **Abdussalam**[*] and Oladapo **Ogidi**[**]

This article postulates a two-step hybrid approach in the control of remedial clauses—*eg*, liquidated damages, forfeiture clauses, deposits, accelerated performance clauses, *etc*. It restates the imperatives for rethinking the strict enforcement of such terms. The currently prevailing strict approach is premised on the view that conditions prevailing at the time of contracting should shape the enforcement of such provisions. In place of that approach, it is proposed that the award and control of pre-determined remedies be parallel to the default common law rules that govern the judicial exercise for determining damages/compensation. In essence, this article argues for the reinstatement of a 'just compensation' standard in the control of such terms; notably, one that takes account of hindsight knowledge or information.

I. Introduction

This paper postulates a two-step approach premised on the just compensation criterion for regulating remedial clauses, mainly liquidated damages and forfeiture clauses in *business-to-business* contracts. The paper aims to critically contribute to the debate in common law jurisdictions on the judicial control of remedial provisions without focusing on any specific jurisdiction. The paper relies primarily on references to the treatment of remedial clauses in England and Wales, Australia, and Canada, given that these jurisdictions have a robust body of case law on the subject. Canadian jurisprudence recognises the centrality of the compensation principle to the regulation of remedial clauses. A Canadian judicial statement confirms this: 'a liquidated damages provision is more likely to be enforced where the claim approximates the amount to which the claimant would otherwise have been entitled according to principles of general contract law'.[1] Yet, that statement needs to be taken more seriously, even in Canada.[2] This is because Canada takes only the *ex-ante* stage seriously but neglects the *ex-post* stage, where hindsight is crucial.[3]

---

* Senior Law Lecturer, University of Otago, Dunedin, New Zealand.

** Engineer at RWE Offshore Wind GmbH, Hamburg, Germany. The authors thank Professor Edwin Peel and Professor Charles Rickett for their comments and advice.

1 *Super Save Disposal Inc. v Blazin Auto Ltd* [2011] B.C.J. No. 2496 at [32] (SC, BC).

2 See Jeff St. Aubin & Rocco Sebastiano, "Liquidated Damages: Canadian Adoption, Divergence and the Necessity for Restatement" (2017) Journal of the Canadian College of Construction Lawyers 139. See also John Enman-Beech, "The Penalty Doctrine in Canada" (2021) 99(3) Can Bar Rev 504.

3 *Liu v Coal Harbour Properties Partnership* [2006] B.C.J. No. 1983 (CA, BC); *Lee v Skalbania* [1987] B.C.J. No. 2502 (SC, BC).

Notwithstanding, Canada still leans towards the just compensation criterion more than other commonwealth jurisdictions, especially the United Kingdom, Australia, and New Zealand. It must be added, however, that the recently prevailing position in Singapore is analogous to that of Canada.[4]

The paper seeks to highlight the imperatives for rethinking the strict enforcement of remedial terms. The prevailing strict approach is premised on the view that conditions prevailing at the time of contracting should shape the enforcement of such provisions.[5] In place of that approach, a two-step hybrid approach is postulated. This approach asserts that the enforcement of pre-determined remedies should be parallel to the default common law rules that govern the judicial exercise for determining compensatory damages. The two-step hybrid approach postulated in this paper is not novel, and it is simply a restatement of equity's stance in treating remedial clauses as adjustable security against default.[6] A model example is found in the Australian High Court decision of *Andrews v Australia and New Zealand Banking Group*.[7] In that case, apart from deciding rightly that the jurisdiction to regulate remedial clauses should not be preconditioned to contractual breach, the court reasoned that where a remedial clause qualifies as a penalty, it should be enforced only to the extent that it represents compensation for the loss suffered by the promisee.[8] This paper's contribution lies in unpacking the compensation principle and mapping its place in the judicial regulation of remedial clauses in line with the remedial expectations of equity. At each step, the component rules of the compensation principle are applied as a filter to determine the extent to which a remedial clause approximates the promisee's loss.

In the first step, the objective is to assess the extent to which the conception or drafting of a remedial clause represents genuine efforts at pre-determining the promisee's risks of loss exposure. In the second step, we are concerned with post-breach matters. There, we apply hindsight knowledge to determine if the pre-estimation of loss considered valid in the first stage equates to or approximates the measure of loss suffered by the promisee. The second stage, as shall be seen, is most critical in avoiding overcompensation as it involves adjusting a remedial term to reflect the proportionate remedial needs prevailing at the time of breach or enforcement. These filtering steps may, however, give way in cases where a promisee can demonstrate a

4 *Denka Advantech Pte Ltd v Seraya Energy Pte Ltd* [2021] 1 SLR 631 at [185]. See also Samuel Teo & Samuel Wittberger, "Refusing to Reinvent the Wheel: The Reaffirmation of the Dunlop Test in Singapore" (2021) Singapore Comparative Law Review 211.

5 *Cavendish Square Holding BV v El Makdessi* [2015] UKSC 67 [*Cavendish Square*]; *Lucio Robert Paciocco v Australia and New Zealand Banking Group Ltd* [2016] HCA 28 [*Paciocco*]; *127 Hobson Street Ltd and Sunil Govind Parbhu v Honey Bees Preschool Ltd and Jason James* [2020] NZSC 53 [*127 Hobson Street*]; *Maxam Opportunities Fund Limited Partnership v Greenscape Capital Group Inc* [2013] B.C.J. No. 2332 at [53] (CA, BC).

6 Theodore Sedgwick, *A Treatise on the Measure of Damages; or, an Inquiry into the Principles which Govern the Amount of Compensation Recovered in Suits at Law*, 2d ed (New York: John S. Voorhies, Law Bookseller and Publisher, 1852) at 398.

7 *John Andrews v Australia and New Zealand Banking Group Ltd* [2012] HCA 30.

8 *Ibid*, at [10], "[i]f compensation can be made to the second party for the prejudice suffered by failure of the primary stipulation, the collateral stipulation and the penalty are enforced only to the extent of that compensation. The first party is relieved to that degree from liability to satisfy the collateral stipulation."

critical commercial justification for incorporating an otherwise over-compensatory term. For reason of space, discussions about the nature of such crucial commercial justifications are not pursued in this article.

It is claimed that the literal enforcement of remedial clauses may correspond with transactional efficiency, freedom of contract and commercial certainty.[9] But that approach risks contravening transactional justice between parties and negatively impacting social welfare potentials or outcomes. Regarding transactional justice, it ignores that the essence of exchange (not being zero-sum transactions) is to enable mutual empowerment through the transfer of economic value between contracting parties.[10] But promisees acquire undue economic windfall when allowed to obtain remedial outcomes that exceed their loss exposures.[11] This is in addition to the fact that most remedial provisions are not products of negotiated contracts but rather outcomes of unilaterally dictated terms,[12] and most promisors (being term-takers) do not consider such terms or their implications to be of vital importance in their decisions to enter contracts.[13] The issue with this is not necessarily the ability of promisees to impose remedial clauses using their bargaining powers. Instead, the promisors do not consider these terms vital to the contract since they are secondary to the primary bargains they enter, even if they are essential to the promisee's contracting considerations.

Regarding social welfare, institutions responsible for designing commercial law rules must pay serious attention to the implications of rules for the sustainability and viability of an economic/commercial ecosystem. By allowing substantial gaps between remedial awards and dynamics in commercial risks, the law furnishes promisees with more than is necessary to incentivise and compensate for engaging in commercial risks.[14] By so doing, the law insidiously enables the proliferation of costs ultimately borne by society. We need to see that by overcompensating or vesting promisees with supra-compensatory rewards, we may weaken struggling firms' financial resilience and bargaining powers, especially small and medium-sized enterprises.[15] Also, we may dampen firms' investment incentives by exacerbating their indebtedness through overcompensation to promisees (or creditors).[16] These social cost effects can become more pronounced in economic crises such as heightened inflationary conditions (where the cost of doing business tends to

---

9 See *Capital Steel Inc v Chandos Construction Ltd* [2019] ABCA 32 (CA, Alta), Wakeling J, dissenting.

10 See *AMEV-UDC Finance Ltd v Austin* [1988] LRC (Comm) 344 at 367, 368 (HC, Cth), Deane J [*AMEV-UDC*]; Mark P. Gergen, "A Defense of Judicial Reconstruction of Contracts" (1995) 71 Ind LJ 45 at 47.

11 See Moshood Abdussalam, "Recalibrating the Governance of Remedial Clauses in Contract Law" (2020) 71(3) N Ir Leg Q 429.

12 See *Blu-Sky Solutions Ltd v Be Caring Limited* [2021] EWHC 2619 at [112]; *Bridge v Campbell Discount Co Ltd* [1962] 2 WLR 439 at 446, 457 (HL, UK) [*Bridge*]; Margaret Jane Radin, *Boilerplate: The Fine Print, Vanishing Rights, and the Rule of Law* (Princeton: Princeton University Press, 2014).

13 Melvin Aron Eisenberg, "The Limits of Cognition and the Limits of Contract" (1995) 47(2) Stan L Rev 211 at 243.

14 Ian R. Macneil, "Power of contract and agreed remedies" (1961-1962) 47(4) C.L.Q. 495 at 500.

15 TT Arvind, "Too big to care?: Financial contracts and the problem of transactional asymmetry" (2021) 84 Law and Contemporary Problems 35 at 43.

16 Ben S. Bernanke & John Y. Campbell, "Is There a Corporate Debt Crisis?" (1988) 1 Brookings Papers on Economic Activity 83 at 90.

increase)[17] or in a deflationary state (when the private cost of repaying debt tends to increase).[18]

An observer may casually interpret this article as arguing for the erosion of the legal force and commercial usefulness of remedial clauses. That would not be a fair interpretation as this paper seeks to heighten the standards for enforcing remedial clauses by aligning remedial rewards with commercial risks. Additionally, a close reading of this article would make it clear to the reader that, in complement to its main thesis, it advances further arguments:

(a) mitigation should be a vital component in the drafting and regulation of remedial clauses;
(b) remedial clauses should only be strictly enforced when they relate to critical commercial interests; and,
(c) enforceable remedial clauses should spare promisees the complexities that would otherwise arise around the component rules of *remoteness* in determining compensation at common law.

The article is divided into three main parts. Part 1 describes the conceptual framework of the article. It outlines the general nature of enforcing remedial clauses informed by the tenor of just compensation. Here, unpacking the compensation principle into component elements is pursued. Further, an overview of the proposed two-step hybrid approach is described. Upon presenting Part 1, we then recommend how the just compensation approach should operate. This shall be pursued in Parts 2 and 3. Part 2 shall discuss how best to assess the validity of the *ex-ante* component of remedial clauses. Part 3 addresses the *ex-post* component of the just compensation approach. The paper shall conclude with the encapsulation of discussions and recommendations made.

II. Just Compensation and Remedial Clauses

Where *just compensation* is the benchmark for evaluating the validity of remedial provisions, due indemnification to promisees is ensured just as common law damages would otherwise permit.[19] The compensation principle, which informs the computation of contract damages, determines whether the gross statement of loss claimed by a promisee approximates his net compensatory entitlement. Therefore, when assessing the validity of remedial clauses, we should defer to the component rules that inform the computation of compensation at common law as a comparator. Anything beyond due compensation or restoration to the promisee should be

---

[17] Peter Bernholz, *Monetary Regimes and Inflation History, Economic and Political Relationships* (UK: Edward Elgar Publishing Limited, 2003) at 10–18.

[18] Atif Mian & Amir Sufi, *House of Debt: How They (and You) Caused the Great Recession, and How We Can Prevent It from Happening Again* (Chicago: University of Chicago Press, 2014) at 18, 19.

[19] See *Recovery Enforcement Inc v T&C Enterprises Ltd* [2021] B.C.J. No. 1691 (Provincial Court, BC) [*Recovery Enforcement*]. See also *Photo Production Ltd v Securicor Transport Ltd* [1980] 2 WLR 283 at 295 (CA, Eng).

considered illegitimate and impermissible except warranted by a solid commercial justification.[20] Such commercial justification cannot be a matter such as loss of profits or increased loss. Instead, it should relate to critical commercial interests such as general business profitability, viability, or survival. Such a critical commercial interest is one that interference with, because of a breach, may seriously unsettle the business of the promisee and not merely profit outcomes, which common law compensatory damages can otherwise sufficiently address.[21] Such critical commercial interests include the need to disincentivise breaches that may: interfere with patents pivotal to the competitiveness of a business,[22] upset a model of doing business,[23] or threaten the continuity of a capital-intensive venture.[24]

The just compensation standard urges adherence to the compensation principle in the governance of remedial provisions, but it does this with a slight difference. While the component rules of causation-in-fact and mitigation are relevant, those of remoteness are excluded. This is because by consenting to remedial terms, a promisor implicitly accepts reparative liability for losses resulting from a breach, thereby eliminating the need to engage the rules of remoteness whose purpose is to determine the extent to which a promisor assumed responsibility for the promisee's loss exposure.[25]

Having excluded the remoteness component, we can now expound on the roles of the other component rules in the hybrid approach propounded in this article. As we know, the component rules of *causation-in-fact* serve to determine the actual or probable nexus between default and loss suffered (where the loss has materialised) or likely to be suffered (where the loss has only accrued but has not materialised).[26] Once a link between default and loss is established, we quantify the measure of damages the promisee is entitled to based on the quality of the connection between default and loss.[27] Where just compensation regulates remedial clauses, *causation-in-fact* play significant roles at the *ex-ante* and *ex-post* stages of assessing validity. At the *ex-ante* stage, they evaluate if the drafting of remedial terms is in proximity to the promisee's commercial realities (or the loss exposures and profit expectations) at the time of contracting. For example, if the promisee stipulates compensation based on their *gross profits* instead of their *net profits*, it would be evident that they have overstated the value of their compensation interest.[28]

---

20 See Eric L. Talley, "Contract Renegotiation, Mechanism Design, and the Liquidated Damages Rule" (1994) 46(5) Stan L Rev 1195 at 1207.

21 See *R v Whatcott* [2019] EWCA Crim 1889.

22 See *Permavent Ltd and Greenhill Industrial Holdings v Stephen John Makin* [2021] EWHC 467 (Ch).

23 See *English Hop Growers Ltd v Dering* [1928] 2 KB 174; *Bartercard Ltd v Myallhurst* [2000] QCA 445 (CA, Qld).

24 See *CRA Ltd and Kelian Ltd v New Zealand Goldfields Investments and Claremont Petroleum* [1989] VR 873 at 875 (SC, Vic).

25 See *Nestor Zachariadis v Allforks Australia Pty Ltd* [2009] VSCA 258 at [148], [149]; *Robophone Facilities Ltd v Blank* [1966] 1 WLR 1428 at 1448 (CA, Eng) [*Robophone*].

26 *Aldgate Construction Co Ltd v Unibar Plumbing and Heating Ltd* [2010] EWHC 1063 (TCC) at [17].

27 *Parabola Investments Ltd v Browallia Cal Ltd* [2010] EWCA Civ 486 at [23]; *Wellesley Partners LLP v Withers LLP* [2016] 2 WLR 1351 at [4] (CA, Eng).

28 *Super Save Disposal (Alberta) Ltd v Shenwei Enterprises Ltd* [2017] ABQB 805 at [13]–[30] (HC, Alta); *Recovery Enforcement*, supra note 19 at [28]–[42].

Another situation where the *causation-in-fact* component would be relevant, *ex-ante*, is assessing whether the remedial clause's conception considers the immediate strength (or otherwise) of the promisee's entitlement to receive performance. That is, whether the contractual right is subject to devaluation by the promisor's leeway in the performance of the contract. Suppose contract interpretation allows the promisee to perform a contract in either *X* or *Y* methods. If wrongful performance following *Method X* would impose a loss of £200 on the promisee, but performance following *Method Y* would impose a loss of £100. Then it follows that a remedial clause flatly stipulating £200 would overestimate the promisee's remedial entitlement.[29] The *causation-in-fact* component is equally relevant at the *ex-post* stage of assessing validity, where the value of the promisee's contractual rights is subject to future contingencies.

We now turn to the relevance of mitigation in policing remedial clauses. But to effectively accentuate the importance of the mitigation component to the compensatory objective, it is first necessary to explain or describe its general nature. As this article does not intend to provide a discourse on the mitigation component, it shall only briefly describe its essence. Mitigation concerns the bilateral sharing or distribution (between contracting parties) of risks and benefits resulting from the actions or non-actions of the promisee in response to default. For this reason, some scholars have rationalised it as ensuring corrective justice between parties, while others consider it advancing distributive justice ends. But the truth is that it serves both objectives, making it challenging to differentiate between either of these ends.[30] Some scholars and judges have sought to explain mitigation as advancing efficiency objectives in that it helps to avoid economic waste.[31] That it mainly prevents the promisee's overreliance on the promisor's contractual undertaking.[32] Although appealing and partly true, this position does not adequately explain mitigation.[33] Some others have sought to rationalise mitigation based on causation. According to them, causal connections describe the essence and nature of mitigation.[34] Yet, others have doubted the viability of causation to explain mitigation.[35]

In this paper, Maharaj's thesis on mitigation is preferred.[36] Maharaj aptly explains that causation cannot explain mitigation; he rightly points out the various

---

29 *Wadham Stringer Finance Ltd v Meaney* [1980] 3 All ER 789 at 797 (HC, Eng) [*Wadham Stringer*].

30 See Ava Sidhu, "The Issue of Betterment in Claims for Reinstatement Costs" (2016) 16 Macquarie Law Journal 127.

31 See Paul J. Bates, "Mitigation of Damages: A Matter of Commercial Common Sense" (1992) 13(3) Adv Q 273. See also Jeffrey G. MacIntosh & David C. Frydenlund, "An Investment Approach to a Theory of Contract Mitigation" (1987) 37(2) UTLJ 113.

32 Robert D. Cooter & Ariel Porat, *Getting Incentives Right: Improving Torts, Contracts and Restitution* (Princeton: Princeton University Press, 2014) at 123–127.

33 See *The Asia Star* [2010] 2 SLR 1154 at [26]–[30] [*The Asia Star*].

34 See Andrew Summers, *Mitigation in the Law of Damages* (2016) (unpublished PhD thesis, Oxford University). See also James Boyd, "Collateral Benefits: Defending the Causal Rationale" (2018) 76(1) UT Fac L Rev 92.

35 See *Six Continents Retail Ltd v Carford Catering Ltd and R Bristoll Ltd* [2003] EWCA Civ 1790 at [18], [19]; Anne Michaud, "Mitigation of Damage in the Context of Remedies for Breach of Contract" (1984) 15(2) RGD 293.

36 Krishneel Maharaj, *An Equitable Approach to Mitigation in Contract* (2020) (unpublished PhD thesis, University of British Columbia, archived at University of British Columbia Library).

inadequacies and contradictions in a causal analysis.[37] Whatever the role attributable to causation in the mitigation analysis, he explains it to be only limited or circumstantial.[38] As he convincingly explains, mitigation is analogous to the workings of equitable principles. This is because mitigation applies according to the specificities of each case. Also, mitigation aims to ensure fairness, reasonableness, and efficiency (regarding wealth maximisation).[39] As he reasons, mitigation is not a rule given that it lacks any clearly defined body of precepts. Still, it is a principle whose concern is allocating the benefits and costs of consequences in a manner consistent with the underlying institutional purpose of contract law and which takes account of contextual peculiarities of contracting parties pre- and post-breach.[40]

He explains that allocating costs and benefits between contracting parties has social interest implications. If reparative liability is imposed on promisors beyond reasonable levels, the aggregate cost would ultimately fall on society.[41] Also, if benefits due to promisees are unfairly credited to promisors or expenses incurred by promisees toward mitigation are uncompensated, society would, in the aggregate, ultimately bear the brunt.[42] Thus, the best way to understand and rationalise mitigation is to see it as a benefit/loss balancing principle informed by advancing social interests. As he rightly submits, while the objective of damages in contract law is to measure up to the 'expectation interests' of the promisee, the law may provide the promisee with only the *necessary minimum measure* of compensation on account of mitigation.[43] The law may not give a promisee compensation equal to his expectation interests either because the promisee's efforts towards mitigation have eliminated that necessity or because the promisee could have taken reasonable steps to reduce his loss exposure but failed to do so.[44] To illustrate, suppose a promisee's expectation interest is £100, but his mitigation possibility is £30. Then by failing to mitigate, the promisee can only get the *necessary minimum measure* of compensation. That is, £100 (the full compensation value) minus £30 (the value of the mitigation possibility), which equals £70 (the *necessary minimum measure* of compensation).

On the obverse, in other cases, limiting the promisee to such necessary minimum measure would be inappropriate because doing so would unfairly transfer economic value, otherwise due to the promisee, to the promisor.[45] Such would be the case where benefits secured by the promisee at a substantial sacrifice of resources are credited towards reducing the promisor's liability. The same would be the case where the promisee suffers a measure of costs to reduce his exposure to loss, where such expenses are not cheap, and it would be unfair to subsidise the promisor.

---

37 *Ibid* at 175–189.
38 *Ibid*.
39 *Ibid* at 223–240.
40 *The Asia Star, supra* note 33 at [32].
41 Maharaj, *supra* note 36 at 252.
42 For example, it could have a chilling effect on a promisee's post-breach entrepreneurial incentives.
43 Maharaj, *supra* note 36 at 208–216.
44 *Ibid*. See also Israel Gilead, "Tort Law and Internalization: The Gap Between Private Loss and Social Cost" (1997) 17 Intl Rev L & Econ 589.
45 Gilead, *supra* note 44; Maharaj, *supra* note 36 at 248–255.

We now shift to the role of mitigation in the governance of remedial clauses. As already stated, the prevailing position is that mitigation is irrelevant to remedial provisions, especially in liquidated damages.[46] But the validity of this view, notwithstanding its predominance, is difficult to justify.[47] This is because it is irreconcilable with the compensatory principle. Mitigation is integral to just compensation.[48] It featured in the control of remedial clauses before the ascendency of the prevailing orthodoxy;[49] and is still implicitly relevant to some remedial clauses, such as forfeitures and deposits, as shall be demonstrated in this paper. So, why does it not currently apply to liquidated damages?

Mitigation is essential to the hybrid method postulated in this article. At the *ex-ante* stage, mitigation ensures that the market realities of the promisees are duly considered in the formulation or stipulation of remedial provisions. For example, mitigation helps assess whether there are promising possibilities for reducing or avoiding loss in the promisee's line of business and whether these possibilities were considered in drafting the clause. Also, at the *ex-post* stage, the rules of mitigation help assess if, after default, the promisee mitigated or could have mitigated its loss.[50] The fact that the promisee mitigated his loss or could have done so may have implications for assessing if, *ex-post*, the remedial clause enables windfall effects to the promisee.

The essence of the just compensation standard is that private remedial determinations should not diverge or be unmoored from the values that underpin default contract law remedies without special justification. To allow that would turn contract law on its head. The purpose of default monetary remedies is to function as secondary rights in substituting a promisee's primary right to receive performance.[51] Therefore, if the value of such secondary rights supersedes those of primary rights, they could make self-interested contractual defaults difficult, punish defaults, or even deprive promisors of profits earned from defaults (when there is no element of unconscionability).[52]

Having described the essence and nature of the proposed hybrid 'just compensation' method, we can now shift to analysing the workings of the first step—the *ex-ante* stage.

---

46 See *Murray v Leisureplay plc* [2005] EWCA Civ 963; *Abrahams v Performing Rights Society Ltd* [1995] ICR 1028 (CA, Eng); *Delaney v Staples* [1992] ICR 483 (HL, UK).

47 See Mir Hossein Abedian Kalkhoran, *Penalty Clauses and Associated Doctrines: A Critical Analysis of the Penalty Doctrine and its Possible Application to the Similar Areas of the Law* (1997) (unpublished PhD thesis, University of Bristol, archived at Explore Bristol Research).

48 Andrew Dyson & Adam Kramer, "There is No "Breach Date Rule": Mitigation, Difference in Value and Date of Assessment" (2014) 130 Law Q Rev 259.

49 See, *eg*, *Watson v Noble* (1885) 13 R 347 at 352 (Court of Session, UK) [*Watson*].

50 See Lisa A. Fortin, "Why there Should be a Duty to Mitigate Liquidated Damages Clauses" (2009-2010) 38(1) Hofstra L Rev 285.

51 *Morris-Garner v One Step (Support) Ltd* [2018] UKSC 20 at [31].

52 See *Medsted Associates Ltd v Canaccord Genuity Wealth (International) Ltd* [2020] EWHC 2952 (Comm).

III. The Ex-Ante Stage of the Just Compensation Method

In this part, we are concerned with whether a remedial clause could, at the date of contractual formation, represent a genuine attempt at pre-estimating the measure of loss(es) likely to follow from default. The analysis of this part of the article shall be pursued following the nature of the default remedies of compensatory damages, which are proposed as the comparator for assessing the validity of remedial terms *ex-ante*.

A. *The Causation-in-fact Component*

In the computation of common law damages, the essence of the causation-in-fact component is to ensure that default alone is not a sufficient basis for receiving compensation.[53] In a technical sense, the component assesses the 'factual' connection between default and the (economic) injury claimed to have resulted from it.[54] Based on the degree of nexus between a wrong and a resulting injury, we may assess the measure of damages due to the victim. But as reality has it, connecting wrongdoing empirically with an injury is often difficult.[55] For this reason, judges often resort to a balance of probabilities to assess whether a past event (*ie*, default) is the cause of loss to the victim.

Where the impact of wrongdoing on loss is assessed as being not less than 51%, a causal connection is considered established.[56] This would make the wrongdoing qualify as the injury's factual cause. However, where the impact of the wrongdoing is assessed to be less than 50%, then it would be said that causation is not established. Where connection is drawn at 51% or more, we then shift to assess damages due to the victim. If the victim's loss has actualised, *eg*, expenses incurred in correcting the loss suffered, the victim gets compensated for the entire value of the loss that has so crystallised. However, where the loss is futuristic (*ie*, losses expected to materialise in the immediate future), the promisee would be entitled to the entire compensatory sum attributable to the breach. For example, if the breach caused the promisee to lose out on a bargain worth £1m, but the promisee established that 'but for' the breach, they would have had the performance capability to earn about 70% of the total sum derivable (*ie*, £1m). The promisee's damages would be £700,000.[57]

However, in other cases where the breach's impact depends on the decisions of third parties (and also where the promisee fails to meet the 51% balance of

---

53 *Extreme Excavating & Backhoe Services Ltd v Scott* [2018] A.J. No. 158 (HC, Alta): "[o]n the other hand, to claim that injury is "obvious" or "self-evident" is to claim that the wrong itself determines the magnitude of damages."

54 Neil Andrews, Andrew Tettenborn & Graham Virgo, *Contractual Duties: Performance, Breach, Termination and Remedies*, 3d ed (London, UK: Sweet & Maxwell, 2017) at 491–507.

55 See *Sprint Electric Ltd v Buyer's Dream Ltd and Aristides George Potamianos* [2020] EWHC 2004 (Ch) at [48] [*Sprint Electric*]. See also *Browning v Messrs Brachers* [2005] EWCA Civ 753.

56 *Perry v Raleys Solicitors* [2019] UKSC 5 at [23] [*Perry*]; *Assetco Plc v Grant Thornton UK LLP* [2020] EWCA Civ 1151 at [150]–[156].

57 *Nicholas Prestige Homes v Neal* [2010] EWCA Civ 1552 at [33]; *Gregg v Scott* [2005] 2 AC 176 (HL, UK) at [9].

probabilities threshold), the applicable rule is different.[58] In such situations, we engage in probabilistic causation, guided by the principle advanced in *Chaplin v Hicks*,[59] to determine the measure of damages the victim is entitled to.[60] This process is often a robust estimation exercise, which involves assessing the positive and negative contingencies characterising the claimant's prospects to otherwise actualise the value claimed as lost due to breach.[61]

When using remedial clauses to pre-determine the measure of loss likely to be suffered, the just compensation method requires that the promisee makes that predetermination in a fashion that corresponds with the *causation-in-fact* component.[62] The promisee cannot pre-determine the value of its loss in a manner that has no bearing on the immediate strength of the contractual rights and the prospects of gains likely to be lost to the default. To illustrate this point, let us first return to common law damages. Suppose a promisee suffers a loss of £800 following a breach. But the promisee would (anyway) have suffered the loss of £400 even if there were no default. The breach is only responsible for £400. In other words, the strength of the promisee's compensatory interest is not more than £400. Therefore, where such a promisee stipulates for £800 as liquidated damages when at the time of contracting, the strength of his compensatory interest is determinable as £400 (or £500), his stipulation would overestimate his compensatory entitlement.

There are case law examples that exemplify this point.[63] A good example is *North West Securities Ltd v Warde*.[64] In that case, the contract price of the hire-purchase contract was about £38,380. The remedial clause entitled the promisee to receive the entire contract price in the event of termination except that credit must be given for sums already paid by the promisor towards instalments, returns to the promisee in proceeds of the sale of the repossessed vehicle and other heads of deduction. Taking account of all the deductible factors that arose, the promisee's supposed entitlement came to £8,753.88. But the promisor resisted paying, arguing that the promisee had terminated the contract in reaction to their default—*ie*, delayed payment. The promisor claimed that its financial obligation to the promisee should not exceed £797.51—the rental sum due on the date the promisee terminated the contract. The Court of Appeal favoured the argument advanced by the promisor mostly because the remedial clause had not attempted a genuine estimation of the different losses likely to be suffered by varying levels or qualities of default. The clause simply allowed the promisee to terminate the contract for various default situations without discriminating between these situations based on the likely implications they could have on the promisee's compensatory interest.

---

58 *Parabola Investments Ltd v Browallia Cal Ltd* [2010] EWCA Civ 486 at [23].

59 *Chaplin v Hicks* [1911] 2 KB 786.

60 S. M. Waddams, "The Valuation of Chances" (1998) 30(1) Can Bus LJ 86. See also Helen Reece, "Losses of Chances in the Law" (1996) 59(2) Mod L Rev 188.

61 See *Trillium Motor World Ltd v General Motors of Canada Ltd* [2017] O.J. No. 3478 at [356]–[359] (CA, Ont); *Jadwan Pty Ltd v Rae & Partners* (2020) 378 ALR 193 at [421], [422] (FC, Cth); *Flame SA v Glory Wealth Shipping* [2014] QB 1080 at [8].

62 See *Azimut-Benetti SpA (Benetti Division) v Healey* [2010] EWHC 2234 (Comm) at [15].

63 *Commissioner of Public Works v Hills* [1906] AC 368; *United Dominions Trust (Commercial) Ltd v Ennis* [1967] 2 All ER 345 (CA, Eng).

64 *North West Securities Ltd v Warde* [1982] 13 NIJB 4 (CA, NI).

The second situation that illustrates this is where the promisor's obligation to the promisee allows leeway in its performance. That is, the promisor's obligation to the promisee is not an absolute or ironclad one.[65] (This situation parallels cases where the *minimum obligation* rule would otherwise have applied in the computation of common law damages).[66] In such a situation, the promisee cannot be said to have appropriately pre-estimated its loss where due regard is not had to the promisee's leeway in performance—notably, the possible devaluing implications for the promisee's compensation interests. For example, suppose the promisee estimated their exposure to loss as £1,000, but a method of performance open to the promisor would have entitled the promisee to not more than £400. The promisee would have overstated their compensatory interest by not incorporating the devaluing implications of the promisor's leeway. Since the damages computation would have considered the devaluation effects at common law, the promisee's pre-estimation of loss should follow suit. But it is vital to remember that determining the scope and quality of the promisor's obligation to the promisee is a function of contractual construction. For example, a determination that a contract was one for sale would generally mean the promisor's obligation is absolute. If it is for a conditional sale or monthly lease, then most certainly, the promisor's obligation is flexible (*ie*, subject to devaluation).[67]

The failure to take devaluation effects into account is closely analogous to a situation prohibited by the rules against penalties where a promisee makes a broad-brush pre-estimation of loss without regard to the varying levels of compensatory interests connected with the contract. Such a situation brings to mind the traditional prohibition of a one-size-fits-all measure of compensation in cases where a default could vary in quality, and the impact of such defaults would be different in degrees.[68] It is concerning such situations that Lord Dunedin said, '[t]here is a presumption (but no more) that it is penalty when 'a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage''.[69] Several 20th century cases confirm and illustrate this point.[70] However, an argument based on the devaluation of remedial entitlement would be improper when the promisor owes an absolute or a defined obligation to the promisee.[71]

---

65 See Ryan Nicholas Howes, "A Right to Choose: A Critical Review and Defence of the Minimum Performance Principle" (2019) 77(2) UT Fac L Rev 164.

66 *Bridge*, *supra* note 12 at 631. See also *Gomez v Olds Discount Co (TCC) Ltd* (1964) 7 WIR 98 (CA, Trinidad and Tobago) [*Gomez*].

67 See *Bridge*, *supra* note 12 at 622.

68 See B. W. M. Downey, "Penalties and Depreciation Clauses" (1962) 25(2) The Modern Law Review 242 at 242. See also John Carter & Elisaheth Peden, "A Good Faith Perspective on Liquidated Damages" (2007) 23 Journal of Contract Law 157.

69 *Dunlop Pneumatic Tyre Company Ltd v New Garage and Motor Company Ltd* [1915] AC 79 at 87. See also *Cooden Engineering Co Ltd v Stanford* [1952] 2 All ER 915 (CA, Eng); *Wayfoong Credit Ltd and Ho Fai v Ho Fai* [1975] HKEC 291 (DC, HK).

70 *Anglo Auto Finance Co Ltd v James* [1963] 1 WLR 1042 (CA, Eng); *Financings Ltd v Baldock* [1963] 2 WLR 359 at 366 (CA, Eng). See also *O'Dea v Allstates Leasing System (WA) Pty Ltd* (1983) 45 ALR 632 (HC, Cth) [*O'Dea*]; *Gomez*, *supra* note 66; *AMEV-UDC*, *supra* note 10.

71 *Wadham Stringer*, *supra* note 29 at 797; *Esanda Finance Corp Ltd v Plessnig* [1989] 63 ALJR 238 (HC, Cth). See also *IAC (Leasing) Ltd v Humphrey* (1972) 126 CLR 131 at 141, 142 (HC, Cth).

B. *The Mitigation Component*

Mitigation is the second component principle of common law damages relevant at the *ex-ante* stage. As stated above, the mitigation principle ensures a fair and equitable bilateral distribution of both the benefits and risks resulting from actions or omissions of the promisee in response to contractual default. At its base, the rule ensures that the promisee gets no more than the *necessary minimum measure* of reparations to remedy its loss. But in other situations, it may be imperative that the promisee gets more than the *necessary minimum measure* (or, in other words, the total value of the promisee's compensation interest).

Suppose a promisee controls 30% market share in a wool market, selling wool at 70 cents per kg. They contracted to sell 2000 kg of wool to the promisor for £1,400. Going by the mitigation principle, if the promisor repudiates, the promisee cannot (barring special factors) insist on the promisor's payment of the contract price or full compensation for their lost bargain. This is because the promisee's market share potential provides them with mitigation possibilities. They can sell the wool to other buyers in the market—even if at a reasonably discounted price (or minimal opportunity cost).[72] The promisee will be entitled to compensation for the incidental costs connected with the breach or for mitigating its impact.[73]

Now, let us consider the matter differently from the lens of remedial terms. Suppose the promisee (with their 30% market share) had incorporated damages or a take-or-pay clause in the contract entitling them to receive, as compensation, 30 cents for each kg of wool not eventually bought owing to repudiation. Such a stipulation would not take the promisee's mitigation possibilities into account. It would allow the promisee to receive £600 for the repudiation in a situation where they could mitigate their loss. Given the promisee's mitigation prospects, their legitimate measure of compensation should not extend beyond the incidental costs incurred in connection with the contract. The non-incorporation of mitigation possibilities into the remedial clause in *O'Dea and Ors v Allstates Leasing System (WA) Pty Ltd*[74] was one of the significant factors that made the Australian High Court decide the remedial clause to be a penalty. Such practice would make promisees either complacent about maximising the market potentials of goods returned by defaulting buyers[75] or enable an undue windfall in situations where the seller has viable opportunities for substitute bargains.[76]

In other cases, the *ex-ante* invalidity of the remedial clause would be informed by its failure to incorporate considerations of expenses or resources that would be saved, which the promisee would have otherwise incurred, had the promisor not defaulted.[77] For example, if the contract price is £200,000, but the promisee would have had to incur overhead costs amounting to about £100,000 to facilitate the trans-

72 See *Charter v Sullivan* [1957] 2 QB 117 (CA, Eng); *Sony Computer Entertainment UK Ltd v Cinram Logistics UK Ltd* [2009] 2 All ER (Comm) 65 at [49] (CA, Eng).

73 See *Tanus Developments Ltd v Vanguard Properties Ltd* [1990] B.C.J. No. 336 (SC, BC).

74 *O'Dea*, *supra* note 70.

75 Jacob S. Ziegel, "The Minimum Payment Clause Muddle" (1964) 22(1) Cambridge LJ 108 at 110.

76 *Tomlinson Pontiac Buick GMC Ltd v Line* [2001] O.J. No. 4009 (Superior Court of Justice, Ont).

77 See *Super Save Disposal (Alberta) Ltd v Shenwei Enterprises Ltd* (2016) ABPC 224 at 224 (Provincial Court, Alta).

action, a remedial clause entitling the promisee to receive £200,000 without regard to the saved expenses of £100,000 would fail to correspond with the mitigation component.[78]

The dynamics would be different for compensatory damages and remedial terms if the promisee (in the hypothetical example above) were a firm operating in a competitive market position (as opposed to possessing a 30% market share). The promisee's mitigation prospects would be ostensibly bleak in such a market situation. Therefore, if they sought damages at common law, they could receive the incremental profits lost because of the breach.[79] Equally, they could stipulate compensation bearing on what could be earned as incremental profits without necessarily accounting for their tenuous mitigation possibilities.

A case that exemplifies this position is the case of *Phonographic Equipment (1958) Ltd v Muslu* ("*Muslu*").[80] In that case, the subject matter of the hire purchase (*ie*, a jukebox) was of such a delicate nature that soon after it got into the possession of buyers, it became at risk of a steep decline in its market value, rendering its resale prospects bleak. The court did not find the 'minimum payment' clause deployed in the contract to be a penalty because it appeared legitimately intended to protect the promisee's interest from the risk of quick depreciation, which the item was exposed to. In *Lombank Ltd v Excell*, the court accepted the position expressed in *Muslu*.[81] Still, it emphasised that the market peculiarities characterising a promisee's trade would determine its mitigation possibilities and, therefore, the imperative to incorporate mitigation considerations into relevant remedial clauses.[82]

It has been argued that the idea that a promisee is expected to mitigate when endowed with market power but not to mitigate when operating in a competitive market is devoid of economic sense.[83] Instead, a promisee's market power should matter for mitigation. It is reasoned that when a promisee lacks bargaining power, they generally find it difficult to dictate contractual terms and conditions to buyers. Therefore, they would find it challenging to impose terms on the buyer to reflect the risk of being exposed to mitigation expenses. On the other hand, where a promisee operates with market power, they usually have better bargaining powers *vis-à-vis* their buyers. For that reason, they could, with relative ease, impose terms to reflect the risk of being exposed to the cost of mitigation in a breach.

While the proposition has a basic economic sense, its soundness *apropos* the compensation principle is weak. This is because it fails to acknowledge the fundamental

---

78 See *Volkswagen Financial Services (UK) Ltd v Ramage* [2007] GCCR 6181 at [22] (County Ct, Eng).

79 *Interoffice Telephones Ltd v Robert Freeman Co Ltd* [1958] 1 QB 190. See also *In re Vic Mill Ltd* [1913] 1 Ch 465 (CA, Eng); *Thompson (W. L.) Ltd v Robinson (Gunmakers) Ltd* [1955] Ch 177 (Chancery Division, Eng).

80 *Phonographic Equipment (1958) Ltd v Muslu* [1961] 1 WLR 1379 (CA, Eng).

81 *Lombank Ltd v Excell* [1963] 3 WLR 700 (CA, Eng).

82 See also *32262 B.C. Ltd v 544006 Alberta Ltd* [1998] A.J. No. 281 at [60]; *Wallace Sign-Crafters West Ltd v Delta Hotels Ltd* [1994] B.C.J. No. 896 at [25].

83 See Victor P. Goldberg, "The Lost Volume Seller in English Law" (2018) Columbia University School of Law, The Centre for Law and Economic Studies, Columbia Law and Economics Working Paper No. 594 <https://scholarship.law.columbia.edu/faculty_scholarship/2325>.

reality that mitigation is a component of the compensation principle.[84] It is an aspect of a secondary right, and it is necessarily a measure of how a person can *respond to breach*. It is not a measure of their ability to *avert breach*, particularly by using contract terms. This goes back to its policy foundation, which is tied to corrective and distributive justice considerations.

It should be noted that even though the party's remedial term qualifies as valid *ex-ante*, it may not qualify as accurate at the *ex-post* stage. This is mostly because a party whose remedial term is reasonable *ex-ante* may yet act opportunistically to secure the fruits of a remedial provision (*ex-post*) when the risk of loss legitimately feared at the time of contracting does not materialise after default.

C. *Summary*

This part demonstrates how the just compensation standard should be a filter in scrutinising the validity of remedial provisions at the *ex-ante* stage. It is shown that a proper assessment of the legitimacy of a remedial clause should involve testing that provision against the component rules of causation-in-fact and mitigation. This would assess how sincere or genuine the drafting or the conception of the provision foreshadows profit possibilities, loss exposure, and loss avoidance possibilities. If a provision fails to measure up as a genuine pre-estimation of loss at this stage, it should be treated as invalid, *ab initio*. However, a provision necessitated by critical commercial justifications may be enforced, notwithstanding that it fails to qualify as a proper pre-estimation of loss. As already stated, such commercial justification cannot be a matter such as loss of profits or increased loss.

IV. The Ex-Post Stage of the Just Compensation Method

The analysis made so far in Part III may, for the most part, be treated as contestable by a reader with opposing views. But the arguments to be made in this part are even more heterodox. At its core, the argument is that the enforcement of remedial terms should be adjusted to the restorative needs and realities existing at the time of enforcement. The most vital motif behind strict enforcement is commercial certainty. But as already demonstrated, commercial certainty does not trump the social cost implications of unearned economic surplus or wealth transfers.

As an extension of the case for a just compensation standard foreshadowed in Parts I and II, it is reiterated that proper regulation of remedial clauses should require the following:

1) that at the time of enforcement, remedial clauses are scaled down to approximate the measure of loss suffered by the promisee;
2) that the promisee makes efforts not to aggravate the implications of default; and

[84] See Jennifer S. Martin, "Opportunistic Resales and the Uniform Commercial Code" [2016] 2016(2) U Ill L Rev 487.

3) where efforts have been made towards loss mitigation, an account is given for gains where transactional justice demands it.

As would be obvious, 1) relates to the *causation-in-fact* element, whose purpose is to ascertain the measure of loss suffered by the promisee. In contrast, 2) and 3) relate to mitigation. Having identified these factors, we shall now shift to addressing each one regarding their roles at the *ex-post* stage.

A. *The Causation-in-fact Component*

This component tracks the quality of the link between contractual default and the measure of loss attributable to the promisor's default. Proponents of the strict approach suggest that so long as a remedial clause qualifies as valid at the contracting stage, we should not, at the enforcement stage, enquire as to whether it has a bearing on the measure of loss suffered.[85] But such a position, it is submitted, should not be accepted.

With hindsight, what parties and judges may assume to be a fair pre-estimation of compensation at the time of contracting may enable undue windfall to the promisee at the time of the breach.[86] Of course, some may argue that the fact that there are possibilities of windfall effects accruing to the promisee should keep us from enforcing remedial clauses as agreed. But such a view ignores the social and dynamic implications of such windfalls.

The system of equity from which the rule against penalties originally emerged assesses the fairness of remedial terms at the time of their enforcement. But the argument often advanced by some is that the jurisdiction to relieve against forfeiture is equity's domain, but that of relief against penalties is that of common law. While equity may assess the fairness of terms at the time of enforcement, the common law assesses the validity of terms at the time of contracting. While such a statement is easy to make, it is generally difficult to apply in practice. One reason is that penalty and forfeiture clauses may be indistinguishable, making a clause qualify as a candidate for review under systems of equity and common law.[87]

Another reason is that even when courts treat a remedial clause as falling under equity's domain, they tend to be driven by the influence of orthodoxy.[88] Even though *ex-post* evidence shows that a remedial clause would furnish an unfair reward to the promisee that is disproportionate to the measure of loss suffered or likely to be

---

85 See *127 Hobson Street*, *supra* note 5; *M & J Polymers Ltd v Imerys Minerals Ltd* [2008] EWHC 344 (Comm); *Cavendish Square*, *supra* note 5; *Paciocco*, *supra* note 5.

86 See the dissenting judgment of Chief Justice Robert Bell in the Court of Appeals of Maryland in *Barrie School v Patch* 933 A.2d 382 (4th Cir, 2007).

87 See *Kay v Playup Australia Pty Ltd* [2020] NSWCA 33 at [91]. See also *Jobson v Johnson* [1989] 1 WLR 1026 (CA, Eng) [*Jobson*]; James Edelman, ed, *McGregor on Damages*, 20d ed (London, UK: Sweet & Maxwell, 2018) at [16-014]; Hugh Beale, ed, *Chitty on Contracts*, 32d ed (London, UK: Sweet & Maxwell, 2017) at [26-216N].

88 See Professor Sarah Worthington QC, "The Death of Penalties in Two Legal Cultures?" in Daniel Clarry, ed, *The UK Supreme Court Yearbook Volume 7: 2015-2016 Legal Year* (UK: Appellate Press) 129.

suffered, courts may enforce the term strictly.[89] There is the recently established orthodoxy that the only reason equity would scale down or depart from the literal enforcement of a forfeiture clause is if there were unconscionability factors on the part of the promisee at the time of enforcement (e.g., sharp practice, fraud or misrepresentation).[90] This attenuates the long-established position that equity has the inherent jurisdiction to relieve against forfeiture in cases where adequate compensation to the promisee is possible.[91] Equity could intervene against forfeiture even in cases where the promisor's default was wilful and repeated, so long as due compensation to the promisee is possible.[92] Unfortunately, this is now heavily contested.

The submission made here is that the bifurcation of regulating rules should be discarded. All remedial clauses should be enforced on account of factors prevailing during enforcement. We should focus on the possibility that promisees can be adequately compensated for the losses likely to be suffered from default. Thus, this calls for the possibility of scaling down remedial clauses to approximate the loss actually suffered by the promisee and avoid or shrink possible windfall effects. If the promisee cannot be adequately compensated, then clauses should be enforced strictly. If the context or circumstance warrants, counter-restitution should be made to the promisor where possible. An excellent example of this would be the tricky situations of deposits analysed below in addressing mitigation. We can illustrate these submissions with a few commonplace scenarios.

Suppose that in 2018, a promisee contracted with a promisor to acquire the latter's company. As part of the acquisition contract, the promisee employs the promisor, and the promisor becomes entitled to 10% of shares in the promisee's company. However, a remedial clause in the agreement prohibits the promisor from privately producing creative works without prior approval by the promisee. Should the promisor act contrary to the terms, he shall forfeit all his shares, and his employment shall be terminated. The forfeiture of his shares shall be without compensation, but necessary payment shall be made for the termination of his employment. Suppose that in 2022, the promisor breached this negative obligation, but the said breach does not in any meaningful way affect the economic interests of the promisee. Should the promisee be allowed to enforce the clause as agreed?

Let us take the position that at the time of contracting, the promisee demonstrated a legitimate interest in incorporating such a high-handed remedial clause. But at the time of enforcement, it would be patently unfair and unreasonable to enforce the clause as agreed, mainly because no loss was suffered due to the breach. Therefore, an approach to enforcement that would adjust the clause to the realities existing at the time of the enforcement would be superior and transactionally just. As a norm the promisee should be entitled to a measure of forfeiture that approximates what they would otherwise have charged to permit for waiver of the term.[93] Otherwise,

---

[89] See *Cadogan Petroleum Holdings Ltd v Global Process Systems LLC* [2013] EWHC 214 (Comm).

[90] *Union Eagle Ltd v Golden Achievement Ltd* [1997] AC 514 (PC, HK); *Omar v El-Wakil* [2001] EWCA Civ 1090; *Celestial Aviation Trading 71 Ltd v Paramount Airways Pte Ltd* [2009] EWHC 3142 (Comm).

[91] *Shiloh Spinners Ltd v Harding* [1973] AC 691 [*Shiloh*]; *Legione v Hateley* (1983) 152 CLR 406 (HC, Aust); *Dillon v Bepuri Pty Ltd* (1988) 4 BPR 9362 (SC, NSW).

[92] *Sanders v Pope* 33 ER 108 at 112; *Stockloser v Johnson* [1954] 2 WLR 439 at 448 (CA, Eng) [*Stockloser*].

[93] *Stockloser*, *supra* note 92 at 449, 450.

the promisee should be entitled to the forfeiture of the said shares but with compensation (based on counter-restitution) given to the promisor, even if at a significant discount to the promisee.[94] The only reason to eliminate counter-restitution to the promisor will be if the promisor has derived a proportional measure of gains from the breach sufficient to exhaust their right to counter-restitution.[95]

Instead, suppose the remedial clause entitled the promisee to buy promisor's shares at a flat 30% discount rate should default arise. In 2018, the value of promisor's shares was £500,000. But in 2022, at the time of the breach, the value of the shares had risen to £1m. If promisee purchased the shares at the said 30% rate, they would abstract up to £300,000 worth of value from promisor (*ie*, £1m/30%) for a breach that resulted in no loss. Such a discount measure would overcompensate promisee and needs to be scaled down.[96]

Other situations depict the need for an *ex-post* adjustment of remedial terms. These situations mainly involve cases where the measure of remedial stipulation exceeds the loss attributable to the default primarily because of changes in the promisee's performance capabilities, profit possibilities or loss exposure since the contract was formed. In situations of this kind, the changes in the promisee's profit possibilities are either due to a general decline in the promisee's market or because the promisee's competitive advantage has since been attenuated. We can illustrate situations of this kind using a representative example.

Suppose promisee, who is in the business of fabricating plumbing pipes, contracted with promisor to supply resin. They signed an exclusive supply contract in 2017. Promisee commanded a 40% market share and had good patronage levels at the time of contracting. Suppose that in May 2019, during the currency of the contract, promisor had difficulties obtaining resins and, as such, breached their contract with promisee. But then, at about the same time as the breach, there was a slump in the construction industry due to construction firms' widespread insolvencies, which would have meant a significant shrink in demand for promisee's pipes. If promisee were to sue for damages for lost profits, it would be difficult to establish causal connections between the breach and its loss of sales/profits on a balance of probabilities. Even if promisee sued based on the authority of *Chaplin v Hicks* for losing a chance to sell pipes, the damages outcomes would remain bleak as its profit possibilities during the breach period would be heavily discounted.[97]

Now, let us consider the scenario differently from a remedial clause lens. Suppose promisee and promisor agreed to a remedial clause to hedge against the risk of default. The remedial clause entitles promisee to receive, as compensation, a sum equalling 50% of the net profits it earned four months before any delay in the resin supply, where such delay is beyond seven days. When conceiving the term, it

[94] See *Lexane Pty Ltd v Highfern Pty Ltd* [1985] 1 Qd R 446 at 447, 452–459 (SC, Qld).

[95] See *Else (1982) Ltd v Parkland Holdings Ltd* [1994] 1 BCLC 130 (CA, Eng) at 140, 141, 144–146; George P. Roach, "Counter-Restitution for Monetary Remedies in Equity" (2011) 68(3) Wash & Lee L Rev 1271.

[96] See *AMEV-UDC*, *supra* note 10 at 370; *Re Computer Room Solutions Pty Ltd* [2021] NSWSC 845 at [79]–[89]. See also *Watson*, *supra* note 49; Michael Lishman, "Penalties and Relief Against Forfeiture of Joint Venture Interests" (2008) 27(2) Australian Resources and Energy Law Journal 219 at 234.

[97] *Sprint Electric*, *supra* note 55 at [100]–[105]; *Perry*, *supra* note 56 at [23].

was estimated that any delay in the supply of resins lasting over seven days would be sufficient to cause promisee a significant setback in production and distribution arrangements. If the clause were to be enforced literally at the time of the promisor's breach, when promisee's sales possibilities were bleak due to a slump in the construction industry, promisee would receive excessive compensation.[98] This is because of the tenuous causal nexus that would exist between default and loss suffered.

The reflexivity of *ex-post* assessment is apparent. It adjusts the promisee's remedial entitlement depending on the needs prevailing at the time of enforcement. If the promisee's loss has dissipated or reduced, it adjusts accordingly by scaling down the remedial award.[99] The only issue is where the measure of loss suffered exceeds the amount or value stipulated. Regarding such situations, it is submitted that to avert difficulty promisees should negotiate for a term that allows the promisee to pursue common law damages in place of its remedial stipulation. It should be borne in mind that remedial clauses may as well be clauses for the limitation of liability.[100] It is submitted that equity should apply to possibly enable the scaling up of remedial liability where transactional justice requires it.

B. *The Mitigation Component*

We now come to mitigation. Here we are concerned with two issues, as foreshadowed above. One is whether the promisee could have made efforts not to aggravate the implications of the promisor's default. And the second is whether transactional justice needs require the promisee to account for gains derived from efforts made (or could have been derived from possible efforts) towards mitigation of loss.

The prevailing orthodoxy that remedial clauses–mainly liquidated damages–obviate mitigation's relevance is difficult to reconcile with equitable rules that suggest otherwise.[101] For example, there is an established rule that where a promisee-creditor refuses to accept offers of repayment of the loan from a promisor-debtor because of delayed repayment, then interests that would otherwise be due to the promisee on the principal sum shall cease to be due.[102] There is also a rule that a promisee must bring deposits into account where he sues for damages further to retain the deposit.[103] Also, there are cases where courts, following equity, have intervened to relieve penalties or forfeitures in the form of retentions of deposits, part payments

---

98 See, *eg*, the concern raised by Adjudicator K.F. Nordlinger in *Northwest Waste Solutions Inc v Bimmer Haus Enterprises Inc* [2011] B.C.J. No. 1953 (Provincial Court, BC).

99 *Jobson*, *supra* note 87; *Peachy v Duke of Somerset* (1724) 1 Stra. 447 at 453.

100 *Eco World – Ballymore Embassy Gardens Company Ltd v Dobler UK Ltd* [2021] EWHC 2207 (TCC) at [111].

101 Nicholas Tiverios advances a similar position in his monograph: Nicholas A. Tiverios, *Contractual Penalties in Australia and the United Kingdom: History, Theory and Practice* (Aust: Federation Press, 2019) at 162–164, 183–193.

102 *Cukurova Finance International Ltd v Alfa Telecom Turkey Ltd* (Nos 3 to 5) [2016] AC 923; *Bank of New South Wales v O'Connor* (1889) 14 App Cas 273 (PC, Vic).

103 *Ng v Ashley King (Developments) Ltd* [2010] 3 WLR 911 (HC, Eng); *Ockenden v Henly* (1858) EB & E 485.

and instalments in circumstances where the promisee has, through alternative transactions, recovered more than was lost due to the promisor's default.[104] The only situations where equity shows reluctance to intervene are when a deposit is an earnest payment or a fair price paid as consideration for the promisee to keep the contract open for the promisor.[105] Even in such cases, equity has consistently demonstrated a willingness to intervene if manifest unfairness is present.[106]

To illustrate the argument, let us first address those cases where the promisee could have avoided aggravating the implications of the promisor's default. Suppose Star Farms is insolvent and, for this reason, considers selling ten acres of the land it owns. On 1 March 2020, they entered a contract to sell the said 10 acres to Hofstra Leisure Ltd, which needs land to build a recreational centre. The contract price agreed was £3m. But on 3 April 2020, Star Farms wrote to repudiate the contract. Hofstra rejected the repudiation and insisted on contractual performance. Star Farms reiterated their repudiation and intimated Hofstra about the willingness of Pilton Farms (an adjoining farm) to sell 10 acres to them (Hofstra) at roughly the same price that they (Star Farm) had agreed to sell to Hofstra. Pilton intimated Hofstra of their willingness to sell, but their price offer was £3.1m. If Hofstra sought common law damages, they most likely would only get compensation for the price differential between the offers of Pilton and Star (*ie*, £100,000). This would be because Hofstra had immediate mitigation possibilities in buying from Pilton at the time of the breach.[107]

Now, let us consider the scenario differently. Suppose in the contract between Star Farm and Hofstra, a liquidated damages clause has been inserted, entitling Hofstra to receive 20% of the contract price as compensation should Star Farms fail to transfer the land as agreed. Of course, at the time of contracting, that sum may have been a proper pre-estimate of the loss likely to be suffered since the Pilton offer was not available to Hofstra as a fall-back alternative. But from the moment Pilton made a genuine offer to sell to Hosftra, Hosftra ceased to have a legitimate interest in enforcing the liquidated damages clause. This is because the fear regarding what the remedial clause was meant to secure against could have been eliminated or alleviated by Hofstra's acceptance of Pilton's offer. For Hofstra to insist on the remedial clause would enable opportunism and a wasteful transfer of wealth to Hofstra. More so, rules allowing such outcomes would discourage renegotiations and embolden promisees to carry on without regard to good faith expectations.

Robophone v Blank[108] is a foremost judicial authority often cited explicitly establishing that remedial clauses obviate the need for mitigation. But then, we should not lose sight of the thoughtful scepticism expressed by Lord Denning in his dissenting judgment, in that case, concerning the supposed irrelevance of mitigation. He expressed his disapproval of promisees taking advantage of remedial clauses to saddle promisors with the effects of their business inefficiencies. The only problem

---

[104] *British Columbia Development Corp v NAB Holdings Ltd (B.C.C.A.)* [1986] B.C.J. No. 656 (CA, BC).

[105] *Polyset Ltd v Panhandat Ltd* [2002] HKCFA 15; *Samarenko v Dawn Hill House Ltd* [2011] EWCA Civ 1445; *Kire Simcevski v Alan Robert Dixon [No 2]* [2017] VSC 531.

[106] *Shiloh*, *supra* note 91; *McDonald v Dennys Lascelles Ltd* (1933) 48 CLR 457 (HC, Cth).

[107] *Strategic Acquisition Corp v Multus Investment Corp* [2017] A.J. No. 800 (CA, Alta).

[108] *Robophone*, *supra* note 25.

with Lord Denning's analysis was that he expressed himself in terms of (the second limb) of the *Hadley v Baxendale*[109] rules that govern remoteness of liability—which is irrelevant to remedial clauses as already explained above. But Lord Denning's reasoning remains sound, nonetheless. This can be gleaned from his statement:

> [i]f the machines were a sound commercial venture, and the plaintiffs, *as good traders*, carried sufficient stock to meet current demands, and no more (adjusting their orders to their manufacturers accordingly), then the plaintiffs would not suffer much damage from Mr. Blank's repudiation [emphasis added]. They could take this machine back into stock, and relet it in a few weeks to one of their customers at the same rental; and when they came to pass their next order to their manufacturers, they would order one less machine than they otherwise would have done. Their damage would be the loss of rental for the few weeks pending the reletting to another customer.[110]

We now come to those cases where transactional justice requires the promisee to account for gains derived (or could otherwise have been derived) from mitigation. Suppose Vendor and Buyer enter into an agreement in which the former would sell to the latter a three-bedroom apartment. They agreed on £900,000 as the purchase price. But when Buyer's facility with her bank went dry, she could not carry on with the purchase. Two weeks after, Vendor entered a substitute sale agreement with another purchaser. The other purchaser agreed to buy for £1.2m. If Vendor still sought to sue for damages, they most certainly would get nothing. This is because Vendor would (or could) have earned £300,000 over what they would otherwise have gained from selling the flat to Buyer.[111]

Consider the matter differently. Suppose Vendor stipulated a remedial clause in the contract requiring Buyer to pay 10% of the contract price as a deposit and that such a sum would serve as agreed damages for Buyer's breach. Two weeks after Buyer's repudiation, the second purchaser pays £300,000 more than Buyer had agreed. Here, it is evident that Vendor's losses are wiped out while also gaining significantly from the substitute sale without taking unusual steps or additional investments to improve the property's value. In such a situation, ignoring hindsight knowledge of Vendor's gains would be unreasonable. Vendor must give an account of the gains, which means Buyer should be freed from the compensatory obligation to Vendor.[112] But the situation would have been entirely different if Vendor had made unusual or additional efforts to attain the substitute sale. In that case, Buyer's compensatory liability is not eliminated.[113] Otherwise, any such attribution would be unfair to Vendor.

---

[109] *Hadley v Baxendale* (1854) 23 LJ Ex 179.

[110] *Robophone*, *supra* note 25 at 1436.

[111] *R. Pagnan & Fratelli v Corbisa Industrial Agropacuaria Limitada* [1970] 1 WLR 1306 (CA, Eng); *Glory Wealth Shipping Pte Ltd v Korea Line Corporation (The Wren)* [2012] 1 All ER Comm 402 (HC, Eng).

[112] See *Aaarons v Advance Commercial Finance Ltd* (1995) 6 BPR 13,911 (SC, NSW).

[113] See *Hussey v Eels* [1990] 2 QB 227 (CA, Eng).

We now come to a situation where a promisee entitled to a remedial clause may not assert his entitlement to the stipulated sum based on unreasonably incurred costs or expenses. Suppose Landlord lets a suite of office rooms to Tenant for 24 months. At the end of the rental term, Tenant leaves the property without any damage to it but does not clean the property when they leave. Landlord instructs their employees to clean the property after Tenant's departure and then notifies Tenant that the cleaning charge is £3,000. But the going rate for the cleaning is not more than £1,000. Going by the compensation principle, Landlord's claim for £3,000 cannot stand as it would be an unreasonable expense incurred to cure the actual cost of breach—which is £1000.[114] The outcome would be the same if Landlord had incorporated a term entitling them to retain Tenant's £3,000 deposit when the market rate for cleaning is £1,000. Enforcing the forfeiture of the £3,000 deposit would be unreasonable and permit the Landlord to keep more than the *necessary minimum* reimbursement—*ie*, £1,000, or an approximate sum.

C. *Summary*

This part demonstrates the workings of the *ex-post* stage of the proposed just compensation standard as a filter in examining the validity of remedial provisions. This stage involves a combination of two factors: an inquiry into the actual loss (or loss exposures) suffered by the promisee and an assessment of the remedial measures sufficient to redress the promisee's loss. A combination of these two factors would determine to what extent the remedial clauses may be scaled down (or upwards if the contract permits such a possibility). However, a remedial provision incorporated to protect a critical commercial interest may yet be enforced as stipulated, even though it exceeds the loss suffered. Again, such commercial justification cannot be a matter of loss of profits or increased loss. Instead, it should relate to critical matters such as the general profitability, viability, or survival of the promisee's commercial ongoings.

V. Conclusions

The arguments pursued in this article can be summarised as follows. A two-stage approach informed by the just compensation criterion should govern the regulation of remedial terms. The first stage should assess the extent to which the pre-estimation of loss represents a sincere or genuine foreshadowing of the promisee's profit possibilities, loss exposure risks, and loss avoidance possibilities. If a term fails to measure up as a genuine pre-estimation of loss at this stage, then it should be treated as unenforceable, *ab initio*. The second stage involves assessing whether the pre-estimation of compensation exceeds the loss (or loss exposures) suffered by the promisee. Where the pre-estimation exceeds the actual default outcomes,

[114] *Sydney Developments Pty Ltd v Perry Properties Pty Ltd* [2016] NSWSC 515.

the stipulation may be scaled downwards to reflect and correct the remedial needs resulting from the default.

The following is a statement of the implications that follow from the thesis of this paper:

(a) remedial terms, especially liquidated damages, do not create debtor-creditor relations between the promisee and promisor;
(b) that there is a need for an *ex-post* (or retrospective) assessment of matters in the place of the currently prevailing forward-looking approach;
(c) that categorising remedial clauses into those of common law and equitable objects is an unsustainable artifice;
(d) that there is a socio-economic imperative to restore the primacy of the 'just compensation' standard in assessing the validity of remedial clauses; and,
(e) that mitigation should be an integral expectation or consideration in the enforcement of remedial terms.