

# **GENERAL PRINCIPLES GOVERNING THE RECOVERY OF LOST PROFITS IN CONTRACT DISPUTES UNDER GEORGIA LAW**

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This paper seeks to introduce the reader to the cases, statutes, and principles of Georgia law that govern the recovery of lost profits that arise out of a breach of contract. Part I of this paper presents the two guiding principles to lost profits recovery: (1) ascertainment and traceability of the lost profits; and (2) contemplation of lost profits by the parties at the time the contract is made. Part II illustrates the application of these two overarching principles to two specific types of contract disputes, sales disputes and construction contract disputes, while also noting specific nuances that may arise under Georgia law in these types of cases.

## **I. The recovery of lost profits damages in general under Georgia law**

Where there is a breach of contract, the amount of damages generally recoverable for breach of contract are those that “arise naturally and according to the usual course of things from such breach and such as the parties contemplated, when the contract was made, as the probable result of its breach.” O.C.G.A. § 13-6-2. Notwithstanding the broad language of these statutes, Georgia law limits the damages recoverable for breach of contract, stating that “[r]emote or consequential damages are not recoverable unless they can be traced solely to the breach of the contract or unless they are capable of exact computation, such as the profits which are the immediate fruit of the contract, and are independent of any collateral enterprise entered into in contemplation of the contract.” O.C.G.A. § 13-6-8. Thus the appropriate measure of damages under Georgia law is

“expectancy” damages, where the court’s aim is to put the non-breaching party “in as good a position as if the [breaching party] had fully performed the contract.” P.M.S. Const. Co. v. DeKalb County, 243 Ga. 870, 872 (1979).

Expectancy damages allow parties in a breach of contract suit to seek loss of future profits or earnings. Jenkins v. Cobb, 47 Ga. App. 456 (1933). Since Georgia law forbids recovery of speculative damages in order "to recover lost profits[,] one must show the probable gain with great specificity as well as expenses incurred in realizing such profits." Kitchens v. Lowe, 139 Ga. App. 526, 531 (1976). Since the profits of many businesses are dependant on many different factors, in general, lost profits are too speculative to allow recovery. Walker v. Crane, 243 Ga. App. 838 (2000) (“generally, expected profits of a commercial business are too uncertain and speculative to afford a basis for damages.”); Ellis v. Major Gas & Oil Co., 154 Ga. App. 34 (1980); Palmer v. Atlantic Ice & Coal Corp., 178 Ga. 405, hn. 2 (1934); Norris v. Pig'n Whistle Sandwich Shop, 79 Ga. App. 369, 373(1) (1949); *see also* Cooper v. National Fertilizer Co., 132 Ga. 529, 535 (1909) (“The profits of a commercial business are dependent on so many hazards and chances, that unless the anticipated profits are capable of ascertainment, and the loss of them traceable directly to the defendant's wrongful act, they are too speculative to afford a basis for the computation of damages.”).

Robert L. Dunn, who has written a leading treatise on lost profits, characterizes lost profits recovery as generally requiring proof of three elements: (1) proximate causation, (2) reasonable certainty as to the amount of profits lost, and (3) foreseeability of the lost profits sought. Robert L. Dunn, *Recovery of Damages for Lost Profits*, Ch. 1. (6th ed. 2005). Mr. Dunn states that proximate cause is a required element in Georgia, citing to Tri-State Systems, Inc. v. Village Outlet Stores, Inc., 135 Ga. App. 81 (1975). *Id.*

at 3. On closer analysis of the Tri-State case, the Court of Appeals never in fact ruled on the appellant's enumerated errors concerning proximate cause, instead finding that the lost profits awarded by the Superior court were not ascertainable or traceable to the acts of the other party and that "the remaining . . . enumerations need not be considered in light of [this] holding." Tri-State, 135 Ga. App. at 84. This is not to say that Dunn is wrong. Indeed, there is a causation element inherent in the lost profits analysis engaged in by the Tri-State court that borders on the but-for causation standard. Id. (lost profits must be "traceable directly to the acts of the other party"); *see also* Hirsch v. J.S. Schofield's Sons Co., 8 Ga. App. 284 (1910) (lost profits recoverable where "the loss of profits is due solely to the defendant's breach of his contract."); Gore v. Malsby, 110 Ga. 893 (1900) (lost profits that are "directly due to the breach of the contract" may be recovered).

However, under Georgia law the causation and certainty elements are blended and treated as a single element by the courts. The result is that for recovery of lost profits under Georgia law two elements must be satisfied: (1) the amount of lost profits must be capable of definite ascertainment and be directly traceable back to the breaching party's acts, Kingston Pencil Corp. v. Jordan, 115 Ga. App. 333 (1967), and (2) the lost "profits were in the contemplation of the parties at the time of the contract." K.A.R. Printing, Inc. v. Pierce, 276 Ga. App. 511, 512 (2005).

#### **A. Proving that lost profits are ascertainable and traceable.**

Recall the Georgia Supreme Court's holding in Cooper v. National Fertilizer Co., 132 Ga. 529, 535 (1909), "[t]he profits of a commercial business are dependent on so many hazards and chances, that unless the anticipated profits are capable of

ascertainment, and the loss of them traceable directly to the defendant's wrongful act, they are too speculative to afford a basis for the computation of damages.” Under Georgia law, these twin requirements – that lost profits be ascertainable and traceable – require some sort of baseline of profitability from which the lost profits can be calculated. A review of Georgia case law reveals two distinct ways to make this calculation.

**a. Ascertaining and tracing lost profits through history of profitability**

The first, and most frequently used, method for calculation of lost profits under Georgia law is calculation from a history of profitability. Where a commercial entity claims lost profits, “recovery can be had only if the business has a proven ‘track record’ of profitability. The jury is not permitted to speculate as to what the allegedly lost profits might have amounted to.” Stern’s Gallery of Gifts, Inc. v. Corporate Property Investors, Inc., 176 Ga. App. 586 (1985) *compare with* Empire Shoe Co. v. NICO Industries, Inc., 197 Ga. App. 411, 413-415 (1990) (plaintiff was unable to recover lost profits where the business did not have a history of profitability, but had historically operated at a loss for a few years prior to the breach) *and* Radlo of Georgia, Inc. v. Little, 129 Ga. App. 530 (1973) (plaintiff “proved no **loss of profits** because he was operating at a **loss**. If it be not so taken, there is no basis for judging what his future performance might have been.”). Therefore, in order to establish that lost profits are ascertainable and directly traceable back to the other party, the lost profit claiming business must have been an established business, proving its lost profits as the deficit between the historical profits realized pre-breach and the profits realized post-breach. Levy Bro. & Co. v. Allen, 53 Ga. App. 246 (1936) (“the anticipated profits of an unestablished future

business are generally too speculative for recovery.”); *see also* S.M.D., L.L.P. v. City of Roswell, 252 Ga. App. 438, 441 (2001) (“where the business has been long established, has uniformly made profits, and there are definite, certain, and reasonable data for their ascertainment, [lost profits] may be recovered at least for a limited reasonable future time, even though they cannot be computed with exact mathematical certainty”).

In Johnson County School Dist. v. Greater Savannah Lawn Care, 278 Ga. App. 110 (2006), the court found that the newly-established plaintiff lawn care company had failed to prove lost profits because the plaintiff “failed to support its claim for lost profits with evidence such that a jury could calculate the damages without resorting to guesswork or conjecture.” *Id.* at 113-14. The evidence proffered by the plaintiff noted the “predecessor[ company]’s history of profitability,” noted that the new company’s president had substantial experience in the industry, noted the profitability forecasted by the predecessor corporation for 2001 (the year before the profits were lost), noted the new company’s losses for 2001, noted the new company’s diversion of marketing funds in 2002, and testified that the new company’s ability to provide lawn care was severely impaired. *Id.* at 113. Nonetheless, the court recognized that at the time of the defendant’s act, the plaintiff was still “absorbing its start-up costs” and this fact, coupled with the facts presented by the plaintiff, was still not enough evidence “to provide the required specificity for calculating an amount of [the plaintiff]’s lost profits directly traceable to the wrongful act by the defendant.” *Id.*; *see also* Moultrie Farm Center, Inc. v. Sparkman, 171 Ga. App. 736 (1984) (where the court found that 15 years of financial records of production levels, product values and expenses as well as a lack of change in managing personnel to be sufficient to prove the plaintiff’s lost profits); Demido v. Wilson, 261 Ga. App. 165, 169 (2003) (lost profits of start up company, “[w]ithout any

records of profitability” were “too uncertain and speculative to be recovered”); Molly Pitcher Canning Co. v. Central of Georgia Railway Co., 149 Ga. App. 5, 11 (1979) (where the company seeking lost profits is a “newly-begun enterprise. . . . there plainly exists no basis upon which a reasonably accurate computation of lost profits might be made, as required by the above-cited cases.”).

While these cases deal with the ascertainment and traceability of lost profits arising from torts, courts use the same standard for assessing claims for lost profits in the breach of contract context. *See also* Marketplace Shopping Center, L.P. v. Basic Bus. Alternatives, Inc., 227 Ga. App. 419 (1997) (the court in a claim for lost profits for breach of contract examined whether the plaintiff’s business had well established profitability); Re/Max of Georgia, Inc. v. Real Estate Group on Peachtree, Inc., 201 Ga. App. 787 (1992) (breach of contract claim for lost profits denied by the court because the plaintiff-corporation was a new business, making their lost profits speculative and not ascertainable).

In Atlanta Gas Light Co. v. Newman, 88 Ga. App. 252 (1953), the court held that lost profits were recoverable because the plaintiff had demonstrated reasonably ascertainable profits through evidence of an established business. In this case, the plaintiff-gas service station operator alleged that the gas supplier had breached its contract by failing to supply the plaintiff’s service stations for a number of days, resulting in lost profits. *Id.* In proving lost profits, the plaintiff offered evidence of his operation of the same service stations for one year prior to the interruption of service; evidence that during that time period the plaintiff operated the service stations at capacity; evidence that but for the interruption caused by the defendants, the service stations would have continued to operate at capacity; evidence that the lost profits

calculated were based upon the difference between operation at capacity and operation during the interruptions; and evidence that the profits during the preceding year had not materially fluctuated. Id. at 254.

This evidence was held to be capable of showing lost profits to a “reasonable certainty,” Id., and, therefore, several types of evidence that prove ascertainable profits can be distilled from this opinion. First, there must be expansive historical evidence of profits that preferably has not fluctuated until the moment of the breaching party’s act. Id.; e.g. Signsation, Inc. v. Harper, 218 Ga. App. 141, 142 (1995) (held that evidence of monthly breakdowns of revenues and costs for the preceding two years were sufficient to make lost profits ascertainable and to support a jury verdict against the defendant). Second, there must be evidence of causation, some evidence that after or during the breaching party’s act, the profits were less than those historically received. Atlanta Gas Light, 88 Ga. App. at 254; e.g. Moultrie Farms, 171 Ga. App. at 739 (plaintiff’s claim that defendant exposed cows to arsenic and caused lost profits was found to be reasonably ascertainable where plaintiff presented evidence comparing the productivity of exposed and unexposed cows).

Finally, Georgia law may require that the same personnel be managing or operating the business during the time period from which the historical data of profitability is taken. Compare R.T. Patterson Funeral Home, Inc. v. Head, 215 Ga. App. 578, 585 (1994) (“Company’s history of actual profits, achieved as an established business ***under plaintiff’s direction*** . . . was an adequate evidentiary foundation for the jury’s award” of lost profits) (emphasis supplied) and Moultrie Farms, 171 Ga. App. at 738-9 (evidence proving lost profits was the fact that there was a “lack of change in management of personnel” over the time period cited as proof of historic profitability

and the period where the tort occurred) *with Johnson County*, 278 Ga. App. at 113 (historic evidence of profits of predecessor business could not establish claim of loss of profits for the business under new owner-plaintiff). This logically flows from the emphasis on non-speculation of damages that exists under Georgia law, the more variables that have been changed between the two comparison periods (pre-breach v. post-breach) the less sure the court is that the breach caused the decrease in profits, making the lost profits claim more speculative.

**b. Ascertaining and tracing lost profits through comparison**

While demonstration of lost profits through a history of profitability is certainly the most commonly accepted method of calculation under Georgia law, an aggrieved party that cannot demonstrate lost profits through a history of profitability may still demonstrate lost profits by comparison. This principle has been most readily accepted in the context of agricultural sales disputes. In *Farmers Mut. Exchange of Baxley, Inc. v. Dixon*, 146 Ga.App. 663 (1978), the purchaser of bad or defective seeds attempts to calculate the profits lost by the failure of the purchased seeds to germinate

by comparison to corn crops grown on land in the same planted field, with the same soil, the same brand of seed, fertilized and cultivated in the same manner, and planted in the same time and under identical weather conditions, then the damages would not be too speculative and conjectural for a jury to determine.

*Id.* at 664; *see also Dixon Dairy Farms, Inc. v. Conagra Feed Co.*, 239 Ga. App. 233, 236 (1999) (“To show lost profits, therefore, Dixon Dairy would have to compare the output of cows kept in the same location and cared for in the same manner, as well as introduce evidence of the expenses it would have incurred.”); *Morey v. Brown Mill. Co.*, 220 Ga. App. 256, 259 (1996) (“damages and lost profits due to any alleged deficiency in the seed

were not shown with any reasonable certainty” where the plaintiff attempted to prove lost profits by comparison because the plaintiff compared “different types of seed which perform differently under the same conditions.”); Lorick v. Na-Churs Plant Food Co., 150 Ga. App. 209, 210 (1979). (Appellant’s lost profits must fail because “[t]here was no testimony that the crops were grown upon the same type of soil, the same kind of seed was used, that weather conditions were similar . . . appellant has not proved his damages, shown his loss of profits or that his alleged injury was caused by appellee’s product.”). This comparison method follows the same logic that is applied in the history of profitability analysis discussed above in that the more factors which are changed between the two compared sets of facts, the less likely the court will find the resulting calculations of lost profits sufficiently ascertainable and traceable to allow recovery.

Alternatively, persons claiming lost profits can also ascertain their lost profits by comparison to subsequent periods of profitability. In Johnston v. Lyon, 173 Ga. App. 524 (1985), an automobile crashed through the plate glass window of a restaurant. The owner of the restaurant sought lost profits that resulted from the front window of the restaurant having to be boarded up over a period of time. Due to the boarded up front window the restaurant had the appearance of being closed, even though the restaurant remained open for business, resulting in a loss of customers and therefore profits. The court allowed the restaurant to recover lost profits holding that “[t]he trier of fact could arrive at a proper measure of damages by comparing the average weekly sales of the restaurant for the period the restaurant was boarded up with the three weeks before the placement of the plywood and the three weeks following its removal.” Id. at 525. While there are few cases employing this technique under Georgia law, it is a viable technique that really operates the same way that a normal history of profitability analysis would

operate and is frequently resorted to by plaintiffs who are unable to show that they had an established business before the breach occurred. *See e.g.* Dunn § 5.8 & 5.9 at p. 433-36.

**B. Proving that lost profits were in the contemplation of the parties at the time of the contract.**

In contract cases, the recovery of lost profits requires not only that they be ascertainable and directly traceable to the breaching party's act, but also that profits are the "immediate fruit of the contract and are independent of any collateral enterprise entered into in contemplation of the contract." McDevitt & Street Co. v. K-C Air Conditioning Serv., Inc., 203 Ga. App. 640, 644 (1992) (where the court found breach of contract causing hotel to have diminished occupancy allowed hotel to recover for lost profits); *accord* O.C.G.A. § 13-6-8. The relevant focus of the court is the contemplation of the parties "at the time of the contract," Authentic Architectural Millworks, Inc. v. S.C.M. Group U.S.A., Inc., 262 Ga. App. 826, 831 (2003); *accord* Commercial & Military Sys. v. Sudimat, C.A., 267 Ga. App. 32, 39 (2004)

Recall that in order to recover lost profits, such profits must be "the immediate fruit of the contract." O.C.G.A. 13-6-8; McDevitt, 203 Ga. App. at 644; Signsation, 218 Ga. App. at 143; Aon Risk Serv., Inc. of Georgia v. Commercial & Military Systems, Inc., 270 Ga. App. 510 (2004). Accordingly, the court infers a contemplation of profits where profits are the principal basis of the contract, making this determination primarily upon the nature of the contract itself. *Compare* McDevitt, 203 Ga. App. 640 (lost profits of general contractor were contemplated and recoverable where subcontractor's failure to timely provide services forced contractor to pay money to the property owner for lost profits, ultimately diminishing the general contractor's profit margin on the

construction work) *and* Atlanta Gas Light, 88 Ga. App. 252 (lost profits contemplated and recoverable for defendant's interruption of gas delivery in breach of a contract between a supplier of gas to gas service station owner/operator) *and* Smith v. A.A. Wood & Son Co., 103 Ga. App. 802, 805 (1961) (lost profits contemplated and recoverable for seller's non-delivery, in breach of a contract, to buyer-manufacturer, who as a result of seller's non-delivery could not manufacture products to be sold for profit) *and* Carter v. Greenville Service Co., 111 Ga. App. 651 (1965) (Lost profits contemplated and recoverable for failure by supplier to deliver goods to dealer which dealer planned to resell goods for a profit) *with* Western Union Telegraph Co. v. Tyre, 58 Ga. App. 43 (1928) (court held that tomato farmer and money wiring company did not contemplate lost profits because tomato farmer failed to inform company of the purpose of the money wiring and the probable consequences that would result from untimely wiring of the funds, even though wiring company's failure to timely wire money caused tomato farmer to be unable to pay striking workers, ultimately causing farmer to be unable to sell tomatoes for profit).

As illustrated by the above cited cases, courts typically find profits contemplated where the contract relationship is supplier/dealer, or in a construction contract where jobs are bid and a fixed profit margin is expected by the aggrieved party. These contracts share the common element that profit, and little else, is the immediate fruit of the contract and the most foreseeable consequence of a failure to perform under the contract is loss of profits for the other side. *See* Carter, 111 Ga. App. at 652 (agreement between supplier/dealer "is sufficient reason for foreseeing that the buyer will make a profit" and thus profits were contemplated). The reason lost profits are so foreseeable is due to the nature of supplier/dealer (and subcontractor/general contractor) contracts,

the dealer is almost entirely dependant upon the supplier for its business to even function, less than full performance will obviously and immediately hinder the dealer's ability to continue to sell the product which the supplier has promised to supply. Contrast this situation with that present in Western Union. There, lost profits were not foreseeable, arguably because the nature of the contract was for services – the wiring of money – and the fact that a failure to wire money in a timely manner would result in lost profits was not foreseeable nor made known to the wiring company. Although sometimes the contemplation of the parties is explicitly stated in the contract, Imaging Systems Int'l, Inc. v. Magnetic Resonance Plus, Inc., 227 Ga. App. 641, 645 (1997) (lost profits not recoverable because the contract specifically precluded recovery of special damages), how foreseeable it is that the profits will be harmed by a breach is the typical way the courts determine the contemplation of the parties at the time of the contract.

**C. Even when seeking lost profits arising from a breach of contract, the non-breaching party still has a duty to mitigate its damages.**

For beach of contract cases, Georgia law imposes upon plaintiffs a duty to mitigate damages, requiring them to “lessen the damages as far as is practicable by the use of ordinary care and diligence.” O.C.G.A. § 13-6-5. Notwithstanding this general rule, “mitigation of damages is in fact not a principle to apply in every case.” J.C. Penney Cas. Ins. Co. v. Woodard, 190 Ga. App. 727, 729 (1989) (Internal quotations removed). Specifically, the duty to mitigate does not apply in cases of fraud, breach of express warranty, Haley v. Oaks Apartments, Ltd., 173 Ga. App. 44 (1984), positive or intentional torts, O.C.G.A. § 51-12-11, where there has been an “absolute promise to pay,” J.C. Penney, 190 Ga. App. 727, and where a tenant abandons a leasehold, Shaheen & Co. v. Dickson, 207 Ga. App. 328 (1993).

Under all other circumstances, the plaintiff in a breach for contract claim is obligated by law to mitigate its damages “as far as is practicable by the use of ordinary care and diligence.” O.C.G.A. § 13-6-5. The phrase “as far as practicable . . .” operates as a condition precedent to the duty to mitigate contract damages. Reid v. Whisenant, 161 Ga. 503 (1926) (the duty to mitigate this rule “is applicable only where the damages can be lessened by reasonable efforts and expense.”). Therefore, the defendant has no duty to mitigate damages where he or she is unable to do so.

One acceptable reason not to mitigate damages is that mitigation is impossible. *E.g.* Resolution Trust Corp. v. Dismuke, 746 F. Supp. 104 (1990) (failure to sell foreclosed property was impossible and did not constitute a failure to mitigate damages because such a sale was prohibited by a bankruptcy stay); City of Dalton v. Smith, 210 Ga. App. 858 (1993) (“As the record is devoid of any evidence that the Smiths failed to mitigate damages or that it was in fact possible to do so, the court correctly refused to give the requested charge”); *but see* Harvey v. J.H. Harvey Co., 256 Ga. App. 333 (2002) (plaintiff’s failure to mitigate damages because it was impossible to obtain another job with the same characteristics as the one from which he was wrongfully discharged was insufficient to defeat charges of failing to mitigate).

Another circumstance that excuses a failure to mitigate damages is impracticability or that mitigation of the damages would cause the mitigating party to incur unreasonable efforts and expense. *E.g.* Carroll County Water Auth. v. L.J.S. Grease & Tallow, Inc., 274 Ga. App. 353 (2005) (relocating the defendant’s affected plant was impracticable because the estimated relocation cost exceeded the value of the business itself, and so defendant cannot be found to fail to mitigate damages by virtue of not relocating the plant); Reid, 161 Ga. 503 (the requirement to mitigate damages “is

applicable only where the damages can be lessened by reasonable efforts and expense”); Haley, 173 Ga. App. 44 (where seller’s property was foreclosed upon due to the fraudulent promise of others to pay a security deed, seller was not required to lessen damages by paying off the security deed and then suing the vendee who assumed the tract of property for the payoff price).

The failure to mitigate damages is typically a defense that is raised by the party alleged to have breached a contract and the burden of proof is on the breaching party to show that the other party could have mitigated its damages. Moreland Auto Shop, Inc. v. TSC Leasing Corp., 216 Ga. App. 438, 441 (1995); Leventhal v. Seiter, 208 Ga. App. 158 (1993). Accordingly, there is no requirement that persons complaining of damages also show in the complaint that he or she had undertaken to mitigate or lessen the damages. Mendel v. Converse & Co., 30 Ga. App. 549 (1923). The allegation that a party has failed to mitigate its damages “must be supported by evidence from which a jury could reasonably estimate the amount by which damages could have been mitigated.” Considine Co. of Georgia, Inc. v. Turner Comm. Corp., 155 Ga. App. 911 (1980) (where the Court refused to give a jury instruction on mitigation of damages where defendant made no attempt to offer evidence of what specific efforts plaintiff could have undertaken in order to mitigate its damages, instead making only a bare allegation of failure to mitigate).

**D. Failure to present evidence of anticipated expenses will bar recovery.**

Another important limitation on the recovery of lost profits has to do with the evidence that must necessarily be presented to recover lost profits. Georgia law draws a firm distinction between lost gross profits and lost net profits, holding that only lost net profits are recoverable. Condeelis v. ABS Artistic Jewelry, Inc., 224 Ga. App. 619, 620

(1997) (“Gross profit is the difference between sales and the cost of goods sold before allowance for operating expenses and income taxes. [cit] Deducting all expenses gives net profits.”). Generally the amount of lost profits recoverable is the **net** profits, not gross profits, as noted by the Court of Appeals in Hixson-Hopkins Autoplex, Inc. v. Custom Coaches, Inc., 208 Ga. App. 820 (1993), which said:

No additional evidence regarding past or projected gross or net profits, expenses incurred for gross profit, or saved expenses was presented during the trial. “There is no evidence of either net profits or data from which Custom Coaches' net profits ... could be calculated.... There is nothing in the record to indicate what expenses Custom Coaches incurred in performing the services ... and thus no evidence from which an inference could be drawn that its net profits had declined....” Grossberg v. Judson Gilmore Assoc., supra [196 Ga. App. 107, 109 (1990)]. See also Bennett v. Smith, 245 Ga. 725, 726, 267 S.E.2d 19 (1980). Therefore, assuming arguendo Custom Coaches' entitlement to lost profits, its proof of lost profits was insufficient as a matter of law.

Id. at 822; *see also* Authentic, 262 Ga. App. at 831 (recovery of lost profits denied because plaintiff “submitted no evidence from which its lost *net* profits could be calculated” (emphasis in original)); *but see* Condeelis, 224 Ga. App. 619 (allowing recovery based upon percentage of gross lost profits, as opposed to net lost profits, where the contract at issue required the commission be based upon the gross profits of the enterprise).

Mere estimation of lost net profits is insufficient; proof of both profits and expenses is required. *See* Comtrol v. H-K Corp., 134 Ga. App. 349, 352 (1975) (barring recovery of lost profits because “plaintiff failed to prove all of its expenses.”); Tri-State Systems, Inc. v. Village Outlet Stores, Inc., 135 Ga. App. 81 (1975) (appellee’s expert who opined that a person in the appellee’s position could expect an increased profit of \$15,000 was insufficient to prove lost profits without supporting factual foundation); Hip Pocket Inc. v. Levi Strauss & Co., 144 Ga. App. 792 (1978) (president’s speculation

of lost profits is insufficient). Indeed, where the plaintiff “fail[s] to put up any evidence of its anticipated expenses, its proof of lost profits [will be] **insufficient as a matter of law.**” (emphasis added) Building Materials Wholesale, Inc. v. Triad Drywall, LLC., 287 Ga. App. 772, 777 (2007); Williamson v. Strickland & Smith, Inc., 263 Ga. App. 431, 435(2) (2003) (where there is presented no evidence of anticipated expenses, proof of lost profits was insufficient for recovery); Authentic Architectural Millworks v. SCM Group USA, 262 Ga. App. 826, 831-832(4) (2003) (evidence of lost gross profits, without evidence of anticipated expenses, was not sufficient to show lost net profits); Shaw v. Ruiz, 207 Ga. App. 299, 304(11) (1993) (lost profits were not recoverable where there was no evidence of anticipated expenses since there is no basis from which net profits could be calculated). However, failure of a party to object to a lack of evidence of anticipated expenses will waive this argument on appeal. Accord Witty v. McNeal Agency, Inc., 239 Ga. App. 554, 562 (1999) (“plaintiffs never made the specific objection urged before this Court for the first time that expenses must be deducted from earnings to establish lost profits. Plaintiffs waived their objection to the admission of evidence of lost profits without proof of expenses for failure to assert such reason before the trial court”).

## **II. Specific instances**

While it is essential to have a grasp on the two core elements of lost profit recovery in Georgia: (1) ascertainable and traceable; and (2) within the contemplation of the parties, it is illustrative to look at lines of cases dealing with particular contract dispute types. By looking at these lines of cases, the subtle points of emphasis and other implied elements to the analysis become apparent. Let us turn then to four common

areas of contract law dispute where the issue of lost profits arises and look for these subtleties.

## **A. Sales**

### **a. Remedies for the Buyer – non-delivery of goods or delivery of non-conforming goods**

Historically, Georgia law did not allow a buyer to recover lost profits for non-delivery of goods, finding such recovery too conjectural, remote, and uncertain. See Cooper v. Young, 22 Ga. 269 (1857) (where evidence of lost profits was held inadmissible against a common carrier of coal who was being sued by the operator of an iron works for non-delivery of coal which resulted in lost profits due to the factory not being able to run). In Butler v. Moore, 68 Ga. 780 (1882), the plaintiff in error sought lost profits for crops which were supposed to be grown on his land, but did not grow because the seed sold to him by the defendant was defective. The Supreme Court articulated the general rule for recovery at that time, citing several cases, stating that a buyer's remedy was generally limited to the difference between the actual value and the agreed price of the goods delivered, plus expenses and interest, and that lost profits were too remote to be recovered. Id. at \*2-3. Notwithstanding its analysis of the case law, the Court held that while reversal of the general rule "might be well addressed to the law-making power, and not to this court . . . we think the court erred in limiting the plaintiff's recovery to the price paid for the seed with interest." Id. at \*4. Accordingly, lost profits are now a remedy available to buyers whose goods are not delivered. See Rogers-Morgan Co. v. Webb, 34 Ga. App. 424 (1925).

Thus, Georgia common law provided lost profits recovery to buyers of goods prior to the state's enactment of the 1972 version of the Uniform Commercial code.

O.C.G.A. § 11-2-713 is based on the 1972 version of the U.C.C. and it sets forth the remedies available to a buyer for the seller's non-delivery of goods or repudiation of a sales contract.

(1) Subject to the provisions of this article with respect to proof of market price (Code Section 11-2-723), the measure of damages for nondelivery or repudiation by the seller is the difference between the market price at the time when the buyer learned of the breach and the contract price together with any incidental and consequential damages provided in this article (Code Section 11-2-715), but less expenses saved in consequence of the seller's breach.

(2) Market price is to be determined as of the place for tender or, in cases of rejection after arrival or revocation of acceptance, as of the place of arrival.

The consequential damages provided for in subpart (1) of this provision are defined in O.C.G.A. § 11-2-715(2):

(2) Consequential damages resulting from the seller's breach include:

(a) Any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and

(b) Injury to person or property proximately resulting from any breach of warranty.

According to Dunn, at 84, the language “had reason to know” reflects the lost damages principle of foreseeability, which under Georgia law is the same as contemplation at the time of the contract. *See Part I.B supra*. This is particularly apparent when looking at the recovery of lost profits by **resellers**. When a purchaser who plans to resell goods suffers from non-delivery, lost profits of his potential resale are only available where the non-delivering seller knows that the purchaser of the non-delivered goods plans to resell the goods.” Carolina Portland Cement Co v. Roper-Strauss-Ferst Co., 33 Ga. App. 511 (1925) *citing* Ladd Lime & Stone Co. v. McDougald

Constr. Co., 29 Ga. App. 116(2) (1922). Recall that lost profits requires that the potential for lost profits be contemplated at the time of the contract, and accordingly, Georgia law requires the seller to have knowledge of the purchaser's intent to resell, in order to satisfy this requirement. See e.g. Glennville Hatchery, Inc. v. Thompson, 164 Ga. App. 819, 823 (1982) (affirming a directed verdict against the appellant seeking consequential damages caused the appellee's delay in delivery of chickens which the appellant planned to resell, so holding because "[t]here was no evidence that appellee was aware, at the time appellant made its demand for possession, that appellant had contracted to sell his second flock of chickens to a third party . . . [and] there was no evidence that damages such as these sought by appellant were within the contemplation of the parties at the time the contract was made.").

Furthermore, O.C.G.A. § 11-2-713's requirement that the damages recoverable be damages "which could not be reasonably prevented by cover or otherwise," reflects the requirement under Georgia law that plaintiffs mitigate damages wherever possible. See Part I.C *supra*. In this vein, Dunn discusses those circumstances where failure to cover will bar recovery of lost profits. Dunn, at 86. Failure to cover will bar recovery of lost profits where

This principle, though not explicitly stated in any Georgia cases, is apparent when reading Georgia's Commercial Code. O.C.G.A. § 11-2-712 reads:

(1) After a breach within Code Section 11-2-711 the buyer may "cover" by making in good faith and without unreasonable delay any reasonable purchase of or contract to purchase goods in substitution for those due from the seller.

(2) The buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages as hereinafter defined (Code Section 11-2-715), but less expenses saved in consequence of the seller's breach.

(3) Failure of the buyer to effect cover within this Code section does not bar him from any other remedy.

....

**Purposes:**

....

Subsection (3) expresses the policy that cover is not a mandatory remedy for the buyer. The buyer is always free to choose between cover and damages for non-delivery under the next section.

However, this subsection must be read in conjunction with the section which limits the recovery of consequential damages to such as could not have been obviated by cover. Moreover, the operation of the section on specific performance of contracts for “unique” goods must be considered in this connection for availability of the goods to the particular buyer for his particular needs is the test for that remedy and inability to cover is made an express condition to the right of the buyer to replevy the goods.

Thus, according to the stated purposes of the statute, a buyer who fails to cover is limited in its ability to obtain consequential damages. This would presumably foreclose the recovery of lost profits, particularly in light of Georgia’s strong stance on mitigation of damages and prohibiting speculation.

Accordingly, it would behoove a purchaser to do its best to cover the goods which were not delivered, considering how unsettled this particular aspect of the Commercial Code appears to be.

**b. Remedies for the Buyer – Breach of Warranty**

While non-delivery of goods is certainly a situation faced by many purchasers where lost profits may be sought, the more common situation where a buyer seeks lost profits is where the goods have been accepted, but unbeknownst to the buyer, the goods are defective and are in breach of a warranty. Typically, this situation involves the buyer accepting the goods shipped and going forward with its business, only to discover the seller’s breach after investing significant amounts of time and sums of money. It is not surprising then that in this situation the aggrieved buyer has more types of recovery

available to it, including recovery of lost profits. The Court of Appeals stated five different spheres of recovery available to the buyer who has purchased goods that are not merchantable:

For a breach of the seller's implied warranty of merchantability a purchaser may recover (a) the reasonable expense of operating or attempting to operate the machine or equipment provided none of the expense is incurred after the discovery of the fact that it could not be made to operate properly, *Cochran v. Jones*, 85 Ga. 678, 683(5), 11 S.E. 811, (b) the reasonable cost of making repairs or correcting defects if incurred by him, *National Sheet Metal Co. v. McKenzie*, 62 Ga. App. 292, 8 S.E.2d 93, or if, by reason of the breach or defects the machine or equipment can not [sic] be made to operate properly by making repairs or correcting defects, (c) the difference between the amount paid and the value of the chattel, *Farmer v. Lee & Smith Mule Co.*, 59 Ga. App. 257, 258(5), 200 S.E. 467, and (d) **loss of profits resulting from the breach, if not speculative**, *Hirsch v. Schofield's Sons Co.*, 8 Ga. App. 284(3), 68 S.E. 1076, and (e) any damage to person or property directly traceable to the breach. (emphasis added)

*Taylor v. Wilson*, 109 Ga. App. 658, 660-1 (1964); *see also* *Lewis v. Bracken*, 97 Ga. 337, (1895) (affirming a district court decision allowing recovery of lost profits where a seller sold to liverymen horses afflicted with a contagious disease, despite the seller's warranty that the sold horses were disease free and the lost profits recovery extended beyond the profits to be made off of the diseased horses which were sold to the plaintiff, but to all lost profits caused by the spread of the disease throughout the business); *Pendley Quality Trailer Supply, Inc. v. B & F Plastics, Inc.*, 260 Ga. App. 125 (2003) ("When a seller breached its warranty, a buyer may recover the difference between the price paid for the goods and the value of the goods delivered. A buyer may also recover for lost profits." (cits. removed))

In breach of warranty cases, the emphasis, in terms of whether the lost profits sought are ascertainable, has less to do with a "history of profitability" and

“contemplation” of lost profits as damages, takes on more of the character of a causation analysis. Unlike damages for failure to deliver to a reseller, whether the seller knows the purpose for which the buyer intends to use the goods does not appear to enter into the analysis. The focus tends to be on the traceability of the breach of warranty, be it a defect (merchantability or fit for purposes), to the damage caused. See e.g. Pendley, 260 Ga. App. at 128 (where the court barred the recovery of lost profits, focusing on whether the plaintiff lost customers “because of the failed wall liners,” which the defendant supplied in breach of its warranties); Farmers Mut. Exchange of Baxley Inc. v. Dixon, 146 Ga. App. 663 (1978) (affirming trial court’s denial of summary judgment that would preclude lost profits and where the court’s holding only discusses causation and the ability to calculate or ascertain the lost profits).

This type of analysis, which is focused on traceability and causation, is more similar to the lost profits analysis engaged in for tort causes of action and this is not surprising considering that frequently breach of warranty claims are accompanied by claims of manufacturer’s negligence. See e.g. Lavoi Corp., Inc. v. National Fire Ins. of Hartford, --- S.E.2d ----, 2008 WL 2468888 (Ga. App. 2008) (plaintiff sued defendant seeking lost profits on theories of “breach of the warranties of merchantability, wholesomeness, and purity [and] strict liability for a manufacturing defect”); Shasta Beverages, Inc. v. Tetley USA, Inc., 248 Ga. App. 381 (2001) (Beverage manufacturer brought action against tea supplier seeking lost profits alleging breach of contract, breach of express and implied warranties, negligence, negligent misrepresentation, and failure to warn); Carr v. Jacuzzi Bros., Inc., 133 Ga. App. 70 (1974) (plaintiff sued manufacturer for sale of defective pumps on both negligence and breach of warranty claims).

One thing which litigants must look out for in claiming lost profits is contract language which forecloses recovery of lost profits. Under Georgia law, a provision disclaiming liability for consequential damages that calls for the exclusion of lost profits damages will be enforced. Imaging Systems Int'l, Inc. v. Magnetic Resonance Plus, Inc., 227 Ga. App. 641 (1997) (clause that specifically prohibited recovery of lost profits and other consequential damages was enforced); White Farm Equipment Co. v. Jarrell & Clifton Equipment Co., 139 Ga. App. 632 (1976). However, where the warrantor causes loss of profits in the course of undertaking its obligations under a warranty, the contract's disclaimer of lost profits will not bar recovery of lost profits. Accord Applying Motors, Inc. v. Todd, 143 Ga. App. 644 (1977) (warranty provision stating that "in no event shall buyer be entitled to recover . . . consequential damages, including . . . loss of profits" would "not bar defendant's counterclaim as it would apply only to loss occasioned by the defective part which was within the warranty and not the negligence in installing it and the consequential damages that followed.") .

While under most circumstances a disclaimer will suffice in limiting a seller's liability for lost profits under a sales contract, the contract's disclaimer will not protect claims that lie in tort that arise out of the seller's duties arising in the execution of the warranty. Furthermore, the U.C.C. will not allow enforcement of a lost profits disclaimer where the contract is unconscionable "as a matter of law." See U.C.C. § 2-719(3) ("Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable."); O.C.G.A. § 11-2-719(3); County Asphalt, Inc. v. Lewis Welding & Eng'g Corp., 444 F.2d 372 (2d Cir.), *cert. denied*, 404 U.S. 939 (1971). However, as discussed in Comment 1 to U.C.C. § 2-719, where both sides in a commercial transaction are able to negotiate terms and seek advice, courts will generally

assumed the parties are sophisticated and therefore disclaimers will rarely be considered unconscionable. A showing of unconscionability under Georgia law is a difficult one to make, requiring a complex analysis of both procedural and substantive unconscionability, the details of which are beyond the scope of this paper. For such a discussion see John K. Larkins, *Georgia Contracts: Law and Litigation*, § 3-15.

**c. Remedies for the Seller – Lost Volume Seller**

When a buyer of goods repudiates a contract, the typical remedy available to the seller is “the profit (including reasonable overhead) which the seller would have made from performance by the buyer, together with any incidental damages provided in [O.C.G.A. §11-2-710], due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.” Franklin v. Demico, Inc., 179 Ga. App. 775 (1986). Simply put, a seller recovers the contract price, plus incidental costs, less the money obtained from resale of the goods. However, Georgia law allows special recovery to certain sellers who are “volume sellers,” allowing them to fully recover the anticipated profit on the repudiated goods, even though the good refused may have been resold. See Unique Designs, Inc. v. Pittard Machinery Co., 200 Ga. App. 647 (1991). In Unique Designs, the plaintiff-seller of lathes sued the defendant-buyer of a wood lathe when the buyer negotiated the purchase of the lathe to a certain price, signed a contract to purchase said lathe, only to use that signed contract to purchase a similar lathe from a competitor of the plaintiff at a reduced price. Id. Despite the fact that the plaintiff resold the lathe to someone else, the court held:

When the seller is a dealer he is entitled to recover lost profits and incidental damages from a repudiating buyer, even though the seller has resold the goods to another buyer at the same price as the original buyer had contracted to pay, for the reason that if the original buyer had not

repudiated, the seller would have been able to make two sales and thus obtain two profits.

“The rationale for the rule for measuring damages in the case of a seller who is a middleman is that the breach by his buyer does not make possible a new sale which the seller could not have otherwise made in which new sale the profit lost upon the sale to the original buyer will be replaced; but rather, results in an irretrievable loss of profits.” 4 Anderson, U.C.C., § 2-708:21 (1983).

Id. at 649.

The key to this recovery is that the seller establishes itself as a “lost volume seller,” which requires the seller to “prove that even though [it] later resold the repudiated contract goods, the sale to the third party would have been made regardless of the buyer’s breach so that the seller would have realized two profits from two sales.”

Id. The key inquiry is the sellers’ ability to provide the product to both the breaching buyer and the resale buyer.” Id. at 649-50 *quoting* Ragen Corp. v. Kearney & Trecker Corp., 912 F.2d 619, 627 (3rd Cir.1990) *and also citing* National Controls v. Commodore Business Machines, 163 Cal.App.3d 688, 209 Cal.Rptr. 636, 643 (1985); Teradyne, Inc. v. Teledyne Indus., 676 F.2d 865 (1st Cir.1982); Snyder v. Herbert Greenbaum & Assoc., 38 Md. App. 144, 380 A.2d 618, 624 (1977).

In Unique, the court noted the seller had “clearly established itself as a ‘lost volume dealer,’” by noting that the seller’s

large inventory of lathes; that the lathe to be delivered . . . was a stock inventory item not specially ordered made or adapted to any specifications on [the defendant’s] part; and that the sale of the . . . lathe to [the other purchaser] would have occurred even if [the defendant] had not repudiated its contract.

Id. at 650. These factors mirror factors in other cases noted by Dunn, and are generally considered the key factors in determining a lost volume seller.

## **B. Construction contracts**

### **a. Calculation of lost profits in construction contracts**

Construction contracts prevent a unique situation in which aggrieved parties frequently seek lost profits. The interdependency of multiple parties upon one another for timely delivery of materials, and timely completion of work, along with the fact that parties to such contracts bid on the work with a preconceived profit margin in mind, leads to lost profits commonly being sought by aggrieved parties.

Under Georgia law:

The basic component of damages recoverable by a contractor when a construction contract is wrongfully breached by the owner is the net profit to which the contractor would have been entitled had full performance of the contract been permitted. That figure is reached by subtracting from the contract price the amount which full performance would have cost the contractor. If performance by either party had begun prior to the breach, adjustments must be made to ensure that the contractor receives the full amount of the profit, but no more. First, there must be added to the profit figure the amount of the contractor's net loss up to the point of the breach. That figure is reached by subtracting from the expenses incurred by reason of the contractor's performance the salvage or resale value of the material left on hand. The sum of those figures (the profit which would have been realized from full performance plus net loss incurred by performance to the date of breach) may in no event exceed the contract price. Second, there must be deducted from the recovery those amounts received by the contractor from the owner as prepayment or progress payment.

*Williams v. Kerns*, 153 Ga. App. 259, 266-67 (1980); *see also Rome Housing Auth. v. Allied Building Materials, Inc.*, 182 Ga. App. 233 (1987) (applying *Williams* to the claims of a subcontractor seeking lost profits). Simply put, the proof of lost profits available to a contractor, or subcontractor, is “calculated by subtracting from the contract price the amount full performance would have cost the contractor.” *Dill v. Chastain*, 234 Ga. App. 770, 771 (1998); *see also Energy Contractors v. Ga. Metal Systems*, 186 Ga. App. 475, 477(2) (1988) (applying the rule to subcontractors). This includes “[a]mounts spent on

materials that the contractor could subsequently use on future projects must be accounted for as would any other expenditures affecting profit.” Dill, 234 Ga. App. at 771. The logic here is the same as the lost volume seller – even though the contractor was able to use the materials purchased for the cancelled project on another project, had both projects proceeded, the materials would have had to have been obtained twice and so the cost of such materials must be deducted from the contract price to ascertain net profits on the cancelled contract.

Dunn notes that another method of measuring the lost profits damages incurred by a contractor is “by a percentage of profit on the contract or costs incurred.” Dunn at § 2.36, p. 184. Dunn further notes that while this is typically shown by expert testimony and while it is common in the construction industry itself, ultimately “it is a less satisfactory method of computation than contract price less cost of completion.” It is unlikely that such computation would be permitted in light of the long line of cases stating that the proper measure of recovery is contract price less cost of completion, see Dill and other cases above.

**b. Issue: damages of the unsuccessful bidder**

One common claim in construction cases is a claim made by the unsuccessful bidding contractor, or subcontractor, that as a result of their wrongful non-selection on the contract they suffered a loss in profits. Simply put, the contractor should have been selected for the job and if they had they would have made X amount of profit off the job; therefore they seek X in damages. Georgia law has roundly rejected this logic and held that the appropriate damages for the unsuccessful bidder is not lost profits, but the cost incurred in preparing the bid. *Accord City of Atlanta v. J.A. Jones Constr. Co.*, 260 Ga. 658(1) (1990); Amdahl Corp. v. Georgia Dept. of Administrative Services, 260 Ga. 690,

(1990) (held that unsuccessful bidder could only recover bid preparation cost and not lost profits) (defendant “argues that lost profits are not recoverable in frustrated-bidders cases, and that, as it is limited to a damage recovery of only bid preparation costs . . . [defendant] is correct that a frustrated bidder may not recover lost profits.”)

**c. Issue: delay damages and lost profits**

Frequently, construction delays are alleged to impact a business’ profits and the aggrieved business will seek lost profits for this loss. While the author has been unable to find many cases under Georgia law discussing this circumstance, Dunn devotes a section to this topic noting that “[l]ost profits damages for *delay* in completion of a construction or manufacturing contract may be recovered by either the owner or the contract, independent of a claim for breach because of inadequate performance.” Dunn at § 2.38, 188.

This was the fact situation encountered by the Eleventh Circuit Court of Appeals in McDermott v. Middle East Carpet Co., 811 F.2d 1422 (1987), where the defendant carpet manufacturing business counterclaimed for lost profits that arose due to a delay in the completion of carpet manufacturing equipment on the part of the defendants. The defendants’ expert witness testified that, based upon arithmetic and geometric models, the companies’ period of profitability was pushed back 8 months. The lost profits computed by the expert, and accepted by the Court, was the difference between full profitability and realized profitability over this 8 month period. Id. at 1426-1428. It is unclear whether the same result would have been reached in a Georgia court in light of the fact that the company in question was (1) an unestablished business, and (2) that during the time period used by the company’s expert as a subsequent history of

profitability the company (a) encountered a fire, and (b) had replaced much of its management. Considering the deep rooted policy against speculation and the facts of this case, this federal case is not particularly persuasive as to Georgia law on the topic of lost profits.

Notwithstanding its persuasiveness, the calculation engaged in by the expert in this case is illustrative of the process engaged in by an aggrieved party seeking lost profits due to delay in completion under a construction contract. That is why it is cited here and is a worthwhile read for those involved in lost profits due to delay situations.

### **III. Conclusion**

Simply put, Georgia law imposes high hurdles on persons seeking damage from lost profits. While the general principles of (1) ascertainability, (2) traceability, and (3) contemplation of the parties, are not particularly abstract or foreign concepts, the real work behind lost profits recovery is in the proof of calculation. The requirement that the party seeking lost profits provide proof of not only future profits, but also future saved costs, that is required in order to ascertain one's lost profits stems from Georgia's well established policy against speculative damages. Accordingly, in order to ensure that one recovers lost profits, the use of an expert, forensic accountant is practically necessary. Thus, proof of lost profits at trial is a team exercise, in which the attorney must actively engage his expert in order to cover his bases as far as presentation of enough evidence, of both costs and profits, into the record such that lost profits are not speculative. Conversely, defense of a lost profits case can best be accomplished through the use of one's own expert who will analyze the other party's work, looking for missed saved costs or showing that the party in question has no history of profitability.