

Special Topics in Small Claims

Contracts

Module 6: Determining Damages in Contract Cases

Objectives --By the end of this session, you will be able to:

- Apply general legal principles governing damages in contract actions;
- Correctly calculate and complete the portions of the judgment form related to pre-judgment and post-judgment interest;
- Apply the law regulating an award of attorneys' fees in contract actions;
- Recognize a liquidated damages clause and determine whether it is enforceable.

Resource Materials—The following resource materials will be used for this section:

- A Basic Introduction to Contract Law
- *Small Claims Law* pp. 84 – 94
- (Handout) *Determining Damages in Contract Cases*
- G.S. 6-21.2: *Attorneys' fees in notes, etc.*
- (Handout) *Rules for Determining Interest on Judgments*

Determining Damages in Contract Cases

Monetary Damages

A party to a contract who is injured by another's breach of the contract is entitled to recover from the latter damages for all injuries and only such injuries as are the direct, natural, and proximate result of the breach or which, in the ordinary course of events, would likely result from a breach and can reasonably be said to have been foreseen, contemplated, or expected by the parties at the time when they made the contract as a probable or natural result of a breach.

Lamm v. Shingleton, 231 N.C. 10 (1949).

Liquidated Damages

Liquidated damages are a sum which a party to a contract agrees to pay or a deposit which he agrees to forfeit, if he breaks some promise, and which, having been arrived at by a good-faith effort to estimate in advance the actual damage which would probably ensue from the breach, are legally recoverable or retainable if the breach occurs. A Penalty is a sum which a party similarly agrees to pay or forfeit but which is fixed, not as a pre-estimate of probable actual damages, but as a Punishment, the threat of which is designed to prevent the breach, or as Security to insure that the person injured shall collect his actual damages. (citations omitted).

Whether a stipulated sum will be treated as a penalty or as liquidated damages may ordinarily be determined by applying one or more aspects of the following rule: '(A) stipulated sum is for liquidated damages only (1) where the damages which the parties might reasonably anticipate are difficult to ascertain because of their indefiniteness or uncertainty and (2) where the amount stipulated is either a reasonable estimate of the damages which would probably be caused by a breach Or is reasonably proportionate to the damages which have actually been caused by the breach.

Knutton v. Cofield, 273 N.C. 355, 361, 160 S.E.2d 29, 34 (1968)

Nominal Damages

Nominal damages are small trivial sums awarded where legal rights have been invaded but no actual loss or substantial injury has been sustained . . . awarded in recognition of the right and the technical invasion resulting from a violation of it.

Woodlief, NC Law of Damages, §3.1 (2015).

Punitive Damages

North Carolina follows the general rule that punitive or exemplary damages are not allowed for breach of contract, with the exception of breach of contract to marry. [citations omitted] The general rule in most jurisdictions is that punitive damages are not allowed even though the breach be willful, malicious or oppressive. . . . Nevertheless, where there is an identifiable tort even though the tort also constitutes, or accompanies, a breach of contract, the tort itself may give rise to a claim for punitive damages.

Newton v. Standard Fire Ins. Co., 291 N.C. 105 (1976).

Duty to Mitigate

The rule in North Carolina is that an injured plaintiff, whether his case be tort or contract, must exercise reasonable care and diligence to avoid or lessen the consequences of the defendant's wrong. If he fails to do so, for any part of the loss incident to such failure, no recovery can be had. This rule is known as the doctrine of avoidable consequences or the duty to minimize damages. Failure to minimize damages does not bar the remedy; it goes only to the amount of damages recoverable.

Oakes v. Wooten, 173 N.C. App. 506 (2005).

Rescission

A rescission implies the entire abrogation of the contract and a restoration of the benefits received from the other party. . . . [It] is not merely a termination of contractual obligation. It is abrogation or undoing of it from the beginning. It seeks to create a situation the same as if no contract ever had existed. . . . Rescission may be by mutual agreement or one party may rescind because of a substantial breach by the other. . . . In either case, a rescission of the contract entitles each party to be placed in Statu quo ante fuit.

Brannock v. Fletcher, 271 N.C. 65 (1967)

The true rule appears to be that rescission or cancellation may properly be ordered where that which was undertaken to be performed in the future was so essential a part of the bargain that the failure of it must be considered as destroying or vitiating the entire consideration of the contract, or so indispensable a part of what the parties intended that the contract would not have been made with that condition omitted.

Jenkins v. Myers, 209 N.C. 312 (1936).

Allowable Interest

Nothing else appearing, the amount of interest that may be legally charged in North Carolina is 8%. GS 24-1. Charging more interest than is legally allowed results in adverse consequences to the seller/lender, which vary depending upon the particular statute involved. See Small Claims Law pp. 96 (as revised) – 97.

Pre-Judgment & Post-Judgment Interest

See Handout *infra*.

Attorneys' Fees

In an action based on contract, attorneys' fees may be awarded only if (1) the contract so provides and (2) attorneys' fees are authorized by statute. In most small claims cases, the authorizing statute is GS 6-21.2 (see copy, attached).

Rules for Determining Interest on Judgments

G.S. 24-5

- (a) Actions on contracts: In an action for breach of contract, except an action on a penal bond, the amount awarded on the contract bears interest from the date of breach. The fact finder in an action for breach of contract shall distinguish the principal from the interest in the award, and the judgment shall provide that the principal amount bears interest until the judgment is satisfied. If the parties have agreed in the contract that the contract rate shall apply after judgment, then interest on an award in a contract action shall be at the contract rate after judgment; otherwise it shall be at the legal rate. On awards in actions on contracts pursuant to which credit was extended for personal, family, household, or agricultural purposes, however, interest shall be at the lower of the legal rate or the contract rate.
- (b) Actions on Penal Bonds:¹ . . .
- (c) Other Actions. - In an action other than contract, any portion of a money judgment designated by the fact finder as compensatory damages bears interest from the date the action is commenced until the judgment is satisfied. Any other portion of a money judgment in an action other than contract, except the costs, bears interest from the date of entry of judgment under G.S. 1A-1, Rule 58, until the judgment is satisfied. Interest on an award in an action other than contract shall be at the legal rate.

Interest is requested in every small claims case for money damages.

I demand to recover the total amount listed above, plus interest and reimbursement for court costs.

<small>Date</small>	<small>Name Of Plaintiff Or Attorney (Type Or Print)</small>	<small>Signature Of Plaintiff Or Attorney</small>
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AOC-CVM-200 (Complaint for Money Owed)

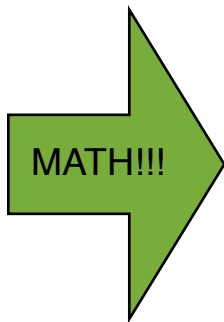
6. I demand to be put in possession of the premises and to recover the total amount listed above and daily rental until entry of judgment plus interest and reimbursement for court costs.		
<small>Date</small>	<small>Name Of Plaintiff/Attorney/Agent (Type Or Print)</small>	<small>Signature Of Plaintiff/Attorney/Agent</small>

AOC-CVM-201 (Complaint in Summary Ejectment)

¹ What is a penal bond? A promise to pay a named sum as a penalty if a condition is not met. A bail bond is a common example, but interest on any performance bond is covered by G.S. 24-5(b). Interest on penal bonds is not the subject of this handout.

Note that a request for pre-judgment interest is built into the small claims forms, much like costs. Furthermore, NC appellate courts have held on a number of occasions that: “Where the amount of damages for a breach of contract is ascertainable from the contract itself, the prevailing party is entitled *as a matter of law* to interest from the date of the breach.”² In other words, the judge is responsible for determining and awarding the appropriate amount of pre-judgment interest based on the evidence, including that contained in the contract itself.

So, how do you determine pre-judgment interest in an action based on breach of contract?



$$\text{Interest} = \text{Principal} \times \text{Rate} \times \text{Time}$$

Principal: This is the amount awarded by the court as damages arising out of breach of contract. Even though the term “principal” may be used to refer to evidence about the original amount of the debt, or to some other amount, remember that G.S. 24-5 deals with interest on judgments.

Rate: If the contract which is the subject of the action contains an agreed-upon interest rate, that same rate is used to determine pre-judgment interest. Otherwise, the legal rate of 8% per annum established by G.S. 24-1 applies.

Time: Period running from date of breach to date of judgment.

How do you determine the date of breach?

² Thomas M. McInnis & Associates, Inc. v. Hall, 318 N.C. 421, 431, 349 S.E.2d 552, 558 (1986).

³ Note that interest rates are frequently stated as annual rates. For shorter time periods, the rate must be converted accordingly. For example, an annual rate of 8% interest converts to a daily rate of 0.00021918.

The general rule is that a contract is breached when the plaintiff acquires the right to bring a lawsuit. In an action for past-due rent, for example, in which the lease contains a 5-day grace period for payment of rent, the date of breach would be on the sixth day; before that time, the landlord had no legal right to bring suit for the past-due amount.

When a contract calls for performance on a particular day, the contract is breached if the party fails to perform on that day. Often, however, date of performance is not so clearly specified. In those instances, the court must determine a reasonable date for performance.

When the evidence supports several possible dates of performance, the court may select the latest date as the date of breach.

Example: *In an action for money owed, a landlord proves that plaintiff failed to pay rent in the amount of \$600 on September 1st and again on October 1st. You hear the case on October 15 and award a money judgment in the amount of \$900.*

- You write \$900 in the judgment form box labeled “Principal Sum of Judgment.”
- Because the lease does not contain any reference to interest, the legal rate of 8% will apply. [NOTE: 8% is the annual interest rate. In order to convert that amount to the daily rate, .08 must be divided by 365.]
- In this case there are two separate breaches, because the tenant missed two payments:


September: $\$600$ (principal) \times $8\%/365$ (daily rate) \times 44 days = \$5.92
October: $\$300$ (principal) \times $8\%/365$ (daily rate) \times 14 days = \$.92

Total prejudgment interest: \$6.84



Hate math? Use the “Judgment Calculator” on the nccourts.org website, found in the drop-down menu labeled “Quick Links.” Or use one of the many free online calculators you’ll find if you do a Google search for “simple interest online calculator.”

In filling out the judgment, the magistrate must separately list the principal sum and the interest due on that amount up to the date of judgment.

<input type="checkbox"/> Costs of this action are taxed to the <input type="checkbox"/> plaintiff.	
Principal Sum Of Judgment	\$
Pre-judgment Interest Not Included In Principal	\$
Attorney's Fees Or Other Damages <i>(when appropriate)</i>	\$
TOTAL AMOUNT	 \$
CERTIFI	

Why does the law require judges to separately identify the principal sum of the judgment and the amount of pre-judgment interest? Because of the interaction of an old rule prohibiting “interest on interest,” and what comes next in G.S. 24-5. . . .

Post-Judgment Interest

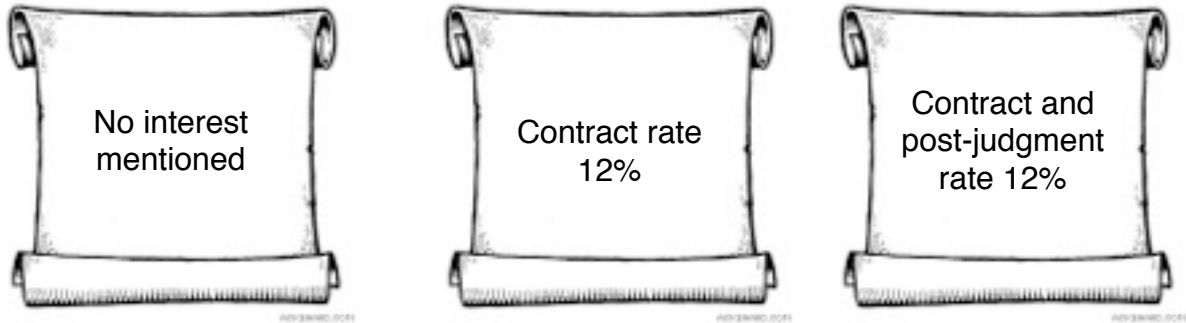
Clerks --not magistrates--are responsible for calculating interest on judgments accumulated between the time the judgment is entered and the time it is paid off (“post-judgment interest”). But magistrates still have an extremely important role to play, arising out of the following statutory provision:

If the parties have agreed in the contract that the contract rate shall apply after judgment, then interest on an award in a contract action shall be at the contract rate after judgment; otherwise it shall be at the legal rate.

Thus a money judgment will gain interest until it is satisfied, subject to two rules:

First, only the “principal sum of the judgment” earns interest. Allowing interest on pre-judgment interest violates the prohibition against “interest on interest.” For this reason, AOC-CVM-400, the small claims judgment form used in “money owed” cases, requires the court to break down the amount awarded into principal and interest.

Second, the law has a “default setting” providing for post-judgment interest at the legal rate. For the contract rate to apply to post-judgment interest, the parties must specifically agree to this in writing. Notice the difference between this rule and the rule that applies to pre-judgment interest.



Pre-J Rate	8%	12%	12%
Post-J Rate	8%	8%	12%

These two rules generate two responsibilities for magistrates. First, the magistrate must separately identify the principal amount of judgment and the amount granted as pre-judgment interest, since only the former gains post-judgment interest. Second, the magistrate must indicate whether the contract between the parties contains a specific provision establishing the rate at which a judgment arising out of the contract will draw interest.

Exception for consumer credit contracts⁴: The last sentence in G.S. 24-5(a) sets out an exception for these contracts, limiting post-judgment interest to the lower of the contract rate or the legal rate.

A magistrate can be sure to provide the clerk with all necessary information by completely filling out the AOC-CVM-400 judgment form:

the case involves a breach of contract and the date of breach is: _____
 the contract provides for pre-judgment interest on damages for breach at the rate of _____% and/or post-judgment interest at the rate of _____%.
 the contract does not provide a specific pre-judgment interest rate.
 the contract does not provide a specific post-judgment interest rate.

⁴ “. . . contracts pursuant to which credit was extended for personal, family, household, or agricultural purposes. . . .”

Pre- and Post-Judgment Interest in Cases Not Involving Contracts

The rules about interest on judgments in cases not based on breach of contract are set out in G.S. 24-5(c). Not surprisingly, these rules are simpler, since the statutory 8% rate applies across the board. Briefly summarized, the statute provides that *a judgment for compensatory damages in an action based on tort draws interest at 8% beginning when the case is filed and continuing until the judgment is satisfied*. In all other cases, pre-judgment interest is not allowed. Applying these rules, then, requires only that a magistrate understand the terms “*tort*” and “*compensatory damages*.”

A person who suffers injury to person or property at the hands of another may bring an *action in tort* to recover damages for the injury. A tort is frequently defined in terms of what it is not: it is not an action based on breach of contract, in which one party to an agreement is complaining that the other party failed to perform as required. Some scholars have said that a tort always involves three essential elements: a duty owed by defendant to the plaintiff, a breach of that duty (whether negligently or intentionally), and a resulting injury to the plaintiff (whether to person or property). Virtually all small claims cases involve either contract or tort.

Compensatory damages are damages calculated to place the plaintiff in as near as may be to the condition s/he would have occupied had the defendant’s tortious action never occurred. Such damages may include compensation for both direct economic loss and less tangible injury such as pain and suffering. Similar to the above discussion concerning the definition of tort, compensatory damages are sometimes defined in terms of what they are not: they are not punitive damages. Furthermore, the general rule is to treat damage awards arising out of statutory penalties as punitive, rather than compensatory, damages. In an action based on unfair or deceptive practices under G.S. 75-1.1, for example, plaintiff’s actual damages are compensatory, but the statutory award of treble damages is not, and thus would not generate pre-judgment interest under G.S. 24-5(c)

Putting It All Together: An Example

Larry Landlord brings an action in summary ejectment seeking (1) possession, (2) \$900 in past-due rent, and (3) \$400 for damage to rental property. The evidence shows the following:

- The parties have an oral lease agreement.
- Tommy Tenant did not pay his monthly rent payment of \$600 on September and he missed another payment on October 1.
- Larry Landlord did not demand the rent from Tommy before filing this action on October 5.

- Tommy got drunk and ran into the metal support for the carport, causing \$400 worth of damage.

You hear the case on October 15.

Your Judgment:

(1) Possession denied because of failure to make proper demand.

(2) Past due rent granted, in the amount of \$906.84. (See p. 3)

(3) Damage to rental property (which is a tort) granted as follows:

\$400 (amount of damage) x 8% (annual legal rate) divided by 365 to determine daily rate x 10 days (beginning when complaint filed and ending when case is heard)

$$\$400 \times 0.00021918 \times 10 \text{ days} = \$0.88$$

(4) Total money judgment \$906.84 + \$400.88 = \$1308.72