NOTES OF CASES

PENALTY OR LIQUIDATED DAMAGES

Two recent decisions of the Court of Appeal in England have turned the spotlight again on the subject of penalties and liquidated damages in the law of contract. In *Alder v. Moore* (1961) 2 W.L.R. 426, a payment of £500 was made to the defendant, a professional footballer, under a policy of insurance taken out by the Association of Football Players' and Trainers' Union with Lloyd's on behalf of their members. The defendant had sustained an injury to one of his eyes and for purposes of the policy was certified totally disabled. Before receiving payment, he signed an undertaking, for which provision was made in the policy of insurance, the undertaking being in the following terms:

> In consideration of the above payment, I hereby declare and agree that I will take no part as a playing member of any form of professional football in the future and that in the event of infringement of this condition, I will be subject to a penalty of the amount stated above.

The amount in question was the £500 that he received under the policy. Less than four months later, the defendant began to play professional football again. The underwriters claimed return of the £500.

One of the defences to the claim set up by the defendant was that the claim was for the enforcement of a penalty. At first instance, Paull J. held that the sum claimed was not a penalty; he held however that the *contra proferentem* rule was applicable in construing the agreement and on this basis gave judgment for the defendant. The plaintiffs appealed.

In *Cambell Discount Co., Ltd. v. Bridge* (1961) 2 W.L.R. 596 there was a hire-purchase agreement for a car the total purchase price of which under the agreement was £482 10s. The hirer paid £105 as initial deposit and followed this up with one monthly instalment. He then found that he could not continue the payments and returned the car to the company, informing them of his inability to continue with the agreement. Under a clause of the agreement, the hirer, if he terminated the agreement before the car became his property, was required to "pay to the owners ... by way of agreed compensation for depreciation of the vehicle such further sums as may be necessary to make the rental paid and payable hereunder equal to two-thirds of the hire-purchase price." The company claimed the sum of £206 3s. 4d. under this clause. The county court held that the sum was a penalty and dismissed the claim. On appeal by the company, the hirer argued that the claim was a penalty, or alternatively, if it was not a penalty, the bargain was harsh and unconscionable and should not be enforced by the court.

The law on penalties and liquidated damages is comparatively free from ambiguity, though, as *Alder* v. *Moore* shows, its application may present difficulties. In a case presenting features justiciable under this branch of the law, the initial question is whether the facts are such as to raise a question of "penalty or liquidated damages." The law was discussed by Lord Dunedin in *Dunlop Pneumatic Tyre Co.,*

Ltd. v. *New Garage and Motor Co., Ltd.* (1915) A.C. 79 where he confined its applicability, or at least discussion of its applicability, to instances of breach of contract. [1] Once a breach was established, then the sum claimed could be tested to see whether it amounted to a penalty or liquidated damages, one of the tests under which the sum was to be construed as being a penalty being where "the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that that could conceivably be proved to have followed from the breach." [2] On the other hand where there was no breach of the contract, it did not fall to be decided whether the sum was a penalty or liquidated damages. Thus in *Associated Distributors Ltd.* v. *Hall* (1938) 1 All E.R. 511 where the agreement provided that in the event of a hire-purchase agreement being terminated under the agreement and not by way of a breach, the hirer would pay a certain sum as compensation to the company, the Court of Appeal held that no question of penalty or liquidated damages arose and that the hirer was liable under the agreement. *Re Apex Supply Co., Ltd.* (1942) Ch. 108 was a similar decision. However, in *Cooden Engineering Co.* v. *Stanford* (1952) 2 All E.R. 915 the Court of Appeal held that the sum itself, in point of amount, could be penal, if it was manifestly excessive, and in such circumstances, the claim would not be enforced irrespective of the fact whether or not a question of penalty or liquidated damages was raised.

The Court of Appeal in *Cambell Discount Co., Ltd.* v. *Bridge* unanimously reaffirmed its previous view that in the absence of a breach of contract no question of penalty or liquidated damages arose. It also held that the sum in itself was not penal, but even assuming that it was, no evidence was adduced that the bargain was harsh and unconscionable. In view of the decision in *Cooden Engineering Co.* v. *Stanford* it is not clear why if the sum claimed was penal in itself, the claim was not held un-enforceable.

Their lordships in *Alder* v. *Moore* were not unanimous. Sellers L.J. appeared to hold the view that no question of penalty or liquidated damages arose because the undertaking signed by the defendant imposed on him no contractual obligation not to play football. As there was no contract, there could be no breach. He preferred the view that the clause of the policy under which the undertaking was given had the effect of making a payment for permanent total disablement conditional and not final. He further thought that the sum claimed was not penal in itself, his words being, "far from being extravagant or unconscionable it is the precise sum which the defendant had received from the underwriters and which he would not have received at all if the future could have been foreseen only four months ahead." He therefore held that the sum was recoverable. Slade J. also took the view that no question of penalty or liquidated damages arose and that the sum was payable on the happening of an event and this event happened when the defendant commenced playing professional football again. Devlin L.J. was strongly of the view that a contractual obligation was imposed upon the defendant by the terms of the undertaking. The breach, he held, occurred when the defendant recommenced playing professional football, and, as this breach occasioned no damage to the plaintiffs, the sum claimed could not be liquidated damages but was a penalty.

1. The present law on this point is succinctly stated by Jenkins L.J. in *Cooden Engineering Co.* v. *Stanford*, where in reference to the question of penalty or liquidated damages he states: "In order to be such, the sum in question must, as I understand the law, be . . . a sum which the hirer undertakes to pay to the owners in the event of, and in respect of, some breach by the hirer of the terms of the hire-purchase agreement. If the agreement contains a provision of that description, and a breach on the part of the hirer ensues, and the owners sue for payment of the sum stipulated to be paid in respect of such breach, then no doubt arises the question of penalty or no penalty, turning on a comparison between the stipulated sum and the damages capable of flowing from the breach or breaches in respect of which the stipulated sum is, according to the terms of the agreement, expressed to be payable".

2. Page 86.

So the Court of Appeal was divided on the initial question whether the facts were such as to give rise to a "penalty or liquidated damages" situation. On this question, no assistance could be obtained from the advice of Lord Dunedin in the *Dunlop Pneumatic* case, supra, for what he said there was applicable only to a situation where the initial question had been decided and what remained to be decided was whether the sum claimed was a penalty or liquidated damages. The position then was that the Court of Appeal necessarily had to construe two documents to see what meaning could be extracted from these. The plaintiffs did not say that the policy or the undertaking did not adequately reflect the agreement entered into by them and the Association of Football Players' Union. They were therefore bound by the words of the policy, if not by those of the form of the undertaking. As to the latter, it is impossible to say, on its wording alone, that no contractual obligation is imposed upon the defendant not to play professional football again. But what, it is submitted is more, on a true interpretation of the clause in the policy under which the undertaking was taken, it cannot be said that the intention was not to take such an undertaking incorporating a contractual obligation. It may well be, as Sellers L.J. stated in his judgment, that the intention behind the policy of insurance was to make provision for a member who was deprived of his livelihood as a professional football player through an injury, but it is difficult not to hold that the effect of the words of the policy were to authorise a permanent ban on a member who claimed and obtained payment under the policy, and that the words of the undertaking, as used in this case, did in fact impose such a ban. On this view, the dissenting judgment of Devlin L.J. may be added to those many others which are classified as dissenting judgments of merit.

KIRPAL SINGH.

3. Page 86.