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Contracts—Damages—Burden of Proof on Elements of Damage in Actions for Breach of a Correspondence School Contract

Where P contracts to build a house for D, and after P has partially performed the contract, D notifies him to stop working, thereby breaching the contract, P's recovery in an action for the breach is limited to the amount of damages he can prove with reasonable certainty.\(^1\) The items comprising his damages are the expenses incurred up to the time of the breach, plus the expected profits on the total contract. This is the normal rule in contracts cases.\(^2\)

However, where P is a correspondence school, and D a person who has contracted to pay for correspondence courses and who subsequently tells P to stop performance, this normal damages rule is only one of three followed in the various state courts. The "Michigan rule" places the burden of proving damages, which includes expenses incurred plus expected profit, on the plaintiff.\(^3\) The "Nebraska rule" purports to


allow the plaintiff-correspondence school, as damages, the contract price less the amount which it saves by virtue of not having to perform the remainder of the contract; but places the burden of proving these "cost savings" on the defendant-student. The third rule is the "Massachusetts rule" which allows plaintiff to recover the entire contract price in all cases on the theory that defendant's promise is an "independent covenant." 7

A closer examination of the "Nebraska rule" discloses that it will result in recovery of the full contract price—the "Massachusetts rule"—in nearly every case. Damages in these cases are always difficult to prove. Showing the proportion of the company's considerable overhead expenses to be borne by this contract, proving the variable expenses incurred on the contract in issue up to the time of the breach, plus showing the reasonable profit on the contract, would be a difficult evidentiary problem, even to one having access to the correspondence school's records. But the normal defendant would have no knowledge of any of the school's records and to him, getting the records to the court in which the action is brought may be just as serious a problem as their interpretation. For the defendant's attorney, often in a different state from that where the records of the company are located, the job is, as a practical matter, impossible, since the amount of money which he can save the defendant is small compared with the costs of litigation. The failure in proof will result in no "cost savings" being shown and recovery of the full contract price by the plaintiff. 9

4 The amount of damages theoretically recoverable by the plaintiff is the same under both the Nebraska and Michigan rules. Suppose a case where the contract price is $100, expenses incurred up to the time of breach $50, and expenses not incurred because of the breach $30, leaving a profit of $20. Under the "Michigan rule," plaintiff should recover past expenses, $50, plus expected profits, $20, totaling $70. Under the "Nebraska rule," plaintiff should recover the contract price, $100, less expenses not incurred because of the breach, $30, also totaling $70. It bears repeating, however, that this is only the theoretical measure of recovery under the two rules, the evidentiary problems of neither party being considered.

5 Int'l Text-Book Co. v. Martin, 92 Neb. 430, 138 N.W. 582 (1912); Int'l Text-Book Co. v. Martin, 82 Neb. 403, 117 N.W. 994 (1908); Int'l Correspondence School v. Crabtree, 162 Tenn. 70, 34 S.W.2d 447 (1931).


7 4 Corbin, Contracts § 983, p. 947 (1951) (An independent covenant is one that is "... not conditioned on performance of an agreed exchange promise in return. ... "). It would seem that the promise of the student to pay money would obviously be dependent upon the promise of the school to furnish lessons under the contract. Professor Corbin agrees with this view in the section cited above defining independent promises.

8 See Int'l Text-Book Co. v. Martin, 92 Neb. 430, 138 N.W. 582 (1912), for an example of an unsuccessful attempt by a defendant, through the testimony of expert witnesses, to show these cost savings.

9 See criticism of "Massachusetts rule," supra note 7.
The purpose of this comment is to put the "Nebraska rule" to a critical test to see if the past decisions seem justified in shifting to the defendant in the correspondence school cases the task of proving plaintiff's cost saving.

There are three arguments generally made in justification of Nebraska's rule. The basic reason for the rule is that because of the near impossibility of proving damages, there will probably be a failure of proof; and rather than have any loss resulting from this fall on an "innocent" plaintiff, it should fall on the defendant "wrongdoer." The cases, however, contain only indirect hints of such an analysis on the part of the courts. However, failure of proof on the issue of damages is something which has often plagued plaintiffs in actions upon contracts, yet the courts have not generally shifted the burden of proof for this reason. In all such cases the breaching party is no less a "wrongdoer" than here. In a field of the law characterized by proof of damage problems very similar to those faced here—the law concerning building contracts—the burden is still placed on the plaintiff to prove the elements of his damages as in the normal contract action.

A second argument sometimes made by the courts is that the addition or loss of one student, when the plaintiff has perhaps hundreds of such contracts, would hardly increase or diminish plaintiff's expenses to any perceptible degree. This argument is, however, basically invalid because it is not necessarily empirically true. When compared to plaintiff's over-all costs of performing all of its contracts, it is true that the savings on one contract may be negligible, but the important factor is found by comparing the cost of completing this one contract

10 The reason for the Nebraska Supreme Court's decisions in the two Martin cases, supra note 5, are not as clear as they might be. Few reasons were given in the opinion, and the Court did not indicate which, if any, it felt were the most important.

11 Note, 34 Iowa L. Rev. 103 (1948).

12 United States v. Behan, 110 U.S. 338 (1884); Wittenburg v. Mollyneaux, 55 Neb. 429, 75 N.W. 835 (1898); Allen, Heaton & McDonald v. Castle Farm Amusement Co., 151 Ohio St. 522, 86 N.E.2d 782 (1949); McCormick, Damages § 142 (1935).

13 "Wrongdoer" seems a harsh term for one who merely breaches a contract. The term has connotations of one guilty of a breach of a moral duty, or duty to society, rather than a mere contractual duty.

14 In both types of contracts, the plaintiff will have fairly large fixed overhead expenses which will need to be apportioned among several contracts other than the one on which action is brought. Both are characterized by having certain variable expenses attributable to the one contract. Also, in both, the evidence to prove expenses and profits must be gleaned from voluminous records.

15 Supra note 1.

with the total costs on that contract, where the savings may very well be substantial. The sum of the cost savings on all of a school’s contracts which have been breached may also be a considerable amount. It would seem, however, that to the Nebraska Supreme Court, the fact that the cost savings will in no case be very substantial might be held to be so obvious as to be a matter for judicial notice. This was a basis of the Nebraska Court’s decision in case,\textsuperscript{17} even though the Court stated there was no evidence before it concerning the amount of the savings. But it does not appear to be a fact so notorious to the reasonable man that the production of evidence would be unnecessary,\textsuperscript{18} and a case involving substantial savings has actually arisen. What the Nebraska Court would do were it faced with a case where the cost savings were actually shown to be substantial,\textsuperscript{19} and no evidence were introduced as to the amount, is a matter for conjecture. That such a case has arisen positively refutes this argument as one generally upholding the “Nebraska rule.”\textsuperscript{20}

There is some indication that the “Nebraska rule” places the burden on the defendant to show cost savings on the theory that this is an element in mitigation of damages to be pleaded and proved by the defendant.\textsuperscript{21} No court which has applied the rule has expressly based its decision on this argument.\textsuperscript{22} This argument begs the question, however, since the main issue is which party should bear the burden of proof, and the mere act of categorizing cost savings as an element in mitigation of damages does not rest the decision on a logically sound basis.

\textsuperscript{17} Intl Text-Book Co. v. Martin, 82 Neb. 403, 117 N.W. 994 (1908).
\textsuperscript{18} It is submitted that in the two Martin cases, supra note 5, the Nebraska Supreme court did not intend to take judicial notice of the fact that “cost savings” will in every case be negligible. The Court may not have viewed its acts in this light. It is possible that, were it pointed out that this was the practical effect of its decision, the Court might be influenced to change the position taken by Nebraska on the burden of proof problem.
\textsuperscript{19} As they were shown to be in Air Cond. Training Co. v. Knouse, 46 So.2d 665 (La. App. 1950).
\textsuperscript{20} The Court of Appeals of Louisiana was faced with that problem in Air Cond. Training Co. v. Knouse, 46 So.2d 665 (La. App. 1950). Previous to this case, the Court had held that cost savings to the plaintiff-correspondence school were negligible, and the Court allowed recovery of the full contract price. See LaSalle Extension University v. Thibodeaux, 155 So. 53 (La. App. 1934). In that case evidence was introduced to that effect by the plaintiff. In the Knouse case, however, the Court recognized the fact that cost savings were considerable, and refused to allow recovery of the full contract price to the plaintiff.
\textsuperscript{21} Intl Text-Book Co. v. Martin, 82 Neb. 403, 117 N.W. 994 (1908); Intl Correspondence School v. Crabtree, 192 Tenn. 70, 34 S.W.2d 447 (1931).
\textsuperscript{22} Nothing was said of the mitigation theory in either of the two cases cited supra note 21, except that the Tennessee Court, without explaining its significance to the decision in question, quoted from a mitigation of damages case during one phase of its argument. The Nebraska Court merely cited one former Nebraska case concerning the burden of proof on elements tending to mitigate a plaintiff’s damages.
Thus it can be seen that each of the arguments23 posed by proponents of the "Nebraska rule" has its equally plausible counter-argument. However, there are other rules from the law of contracts and evidence that seem to swing the balance against the "Nebraska rule" and weaken the position of those jurisdictions following it.

(a) Where the facts necessary to prove a given issue are primarily within the knowledge of one party, that party will generally have the burden of proof on the issue.24 This rule is followed in Nebraska to the point of actually shifting the burden of proof from one party to the other for this reason alone.25 Here the correspondence school has all the records necessary to compute the amount of its costs and expected profits, and has in its employ the personnel to interpret this evidence.26 Under this theory, therefore, the burden of proving the measure of damages would seem better placed on the plaintiff.

(b) Most jurisdictions, Nebraska included, allow either party to a contract to stop performance of the contract by the other party and have his damages assessed as of that time.27 The other party is not then allowed to increase the breaching party's damages by continuing to perform his part of the contract.28 A rule which allows recovery of the full contract price by the plaintiff, regardless of the stage of performance at which he was asked to stop, would seem to be in direct

23 An additional theory upon which the Nebraska Court might have relied in its decision in the Martin cases is that the contract was an "entirety," in which case the burden would be on the defendant to prove plaintiff's cost savings. Professor Williston has criticized this theory, see 5 Williston, Contracts § 1352 (Rev. ed. 1937), pointing out that it can have application only in the case where the student has paid his money, then breached the contract, and brings action for the return of his payments.


26 The Nebraska deposition and discovery rules, Neb. Rev. Stat. §§ 25-1267.01 to 25-1267.44 (Cum. Supp. 1951), provide a method by which defendant's attorney could obtain this information from the plaintiff. As pointed out, however, this process is too costly compared with the amount saved to the defendant to be of any practical use in these cases.

27 Hale v. Hess, 30 Neb. 42, 46 N.W. 261 (1890); Rockingham County v. Luten Bridge Co., 35 F.2d 301 (4th Cir. 1929); Int'l Text-Book Co. v. Jones, 166 Mich. 86, 131 N.W. 98 (1911); 5 Corbin, Contracts § 1038 (1951).

28 The equity of this rule can easily be illustrated by the case where the contract calls for payment of many thousands of dollars. The party who has contracted to pay the money may be able to get out of paying thousands of dollars—representing expenses which the plaintiff does not have to incur—by breaching the contract and paying his damages at that time. Where a party knows he will not be able to meet the total contract price, this is a very valuable right. To hold as the Massachusetts and Nebraska rules do amounts to giving specific performance of the contract in every case. See Gardner, An Inquiry Into The Principles Of The Law of Contracts, 46 Harv. L. Rev. 1, 16 (1932).
conflict with the spirit of this rule. Allowing plaintiff full recovery takes away the only value this right has to the defendant, that of saving him money.

(c) The aim of giving the plaintiff damages in contract cases is to put him in as good a position as he would have been had the contract been performed—labeled “compensatory” damages.\(^2\) In no case will more than mere compensation be given, and Nebraska cases contain particularly strong language to this effect.\(^3\) But in these correspondence school cases, recovery by the plaintiff of the full contract price will amount to more than mere compensation in virtually every case, since it is admitted that there will be some savings to the plaintiff, even though the amount of the savings is in dispute.

In the light of the conflict between the “Nebraska rule” and the general rules of contract law set out above, the position of the rule—on the opposite side of the fence from the normal burden of proof rule on elements of damage—would not seem to be justified. In addition, there are considerations of policy which further question the favoritism shown correspondence schools under the “Nebraska rule.” Even a brief consideration of the circumstances under which a correspondence school contract is signed illustrates the bargaining inequality of the parties. There is no bargaining as to terms, the contract being made up by the school and sent to the student who signs with no chance to alter the terms. Also, although the law may assume the contrary, it would seem that persons who contract to pay for these courses would seldom understand the consequences of their act.\(^3\) Rarely will the student know the law governing the interpretation and enforcement of his contract, but most certainly the school will know.\(^3\)

While attention has been focused on the hardships to the defendant-student in the cases, the plight of the correspondence school which


\(^3\) A cursory study of correspondence school advertisements will disclose that many of them are directed at persons without even a high school education.

\(^3\) There is a general public policy, recognized by the courts, favoring the one party to a contract who had nothing to do with drafting its terms. An example of this feeling on the part of the courts is evidenced by the rule that where there is doubt as to which of two possible and reasonable meanings should be adopted, the court will choose the one which is less favorable in its legal effect to the party who chose the terms of the contract. See Northern Pacific R.R. v. Twohy Bros. Co., 95 F.2d 220 (9th Cir. 1938); Lyman-Rickey Sand & Gravel Co. v. State, 123 Neb. 674, 243 N.W. 891 (1932); Restatement, Contracts § 236(d) (1932). This rule has been described as one “... of public policy, generally favoring the under dog.” 3 Corbin, Contracts § 559, p. 155 (1951).
must sue if it is to collect on its contract should not be forgotten. The fact remains that under the "Michigan rule," damages are extremely difficult for the school to prove, as well as the student. A suggestion that the school should bear this burden of proof, though backed by all of the principles heretofore set out, is not fully justified without a consideration of the practical consequences of such a suggestion. It may be that the recovery to the school would not justify the school's litigation expenses, so that recovery, as a practical matter, would be barred by placing the burden of proof on the school, as does the "Michigan rule." Although no figures are available as to the number of these contracts breached, the number could conceivably be high. And where a school brings action on the same contract a number of times, methods and means of proof could probably be worked out that would greatly simplify the problem of litigation and possibly lower litigation expenses to the extent that the school will profit by following a policy of suing on the contracts.

However, even if the correspondence school cannot, under the "Michigan rule," sue on its contracts and recover enough to pay costs of litigation, it is submitted that the "Nebraska rule" is not thereby justified. First, the contract will normally call for a down payment to be made by the student before the course starts, plus the making of periodic payments. The amount represented by these payments may well cover the costs on this contract as well as a portion of the expected profits. And the materials and labor thus saved on one contract may be directed to another profit making contract. Second, the law has long provided a remedy for persons entering a contract in which damages will be difficult to prove—a liquidated damages clause. A valid liquidated damages clause, i.e., one that does not amount to a

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33 No business organization contacted was able to suggest where such information might be found.

34 An example of only one of the things which a school might do is to provide in its contracts that the law of its own state will govern interpretation and enforcement of the contract. Thus the problem of proving damages under the laws of different jurisdictions need not be met. But cf. notes 31 and 32 supra.

35 In none of the cases found concerning correspondence school contracts did the facts show that a different method of payment was employed.

36 A further policy consideration favoring a change in the rule followed in Nebraska is that the school is in a position to spread the loss on this contract among its other contracts. If the school knew that it would not be able to collect fully on contracts which were breached, it could take this into consideration when establishing the prices for its courses.

37 Correspondence school contracts are analogous to contracts to sell goods to the extent that the materials and labor not expended on the breached contract may still make a profit for the seller—the correspondence school—when diverted to use in another contract. Actually, therefore, the proportion of the profit on the breached contract represented by the amount of unused materials and labor is not lost to the school.

38 For a history of the law of liquidated damages, see McCormick, Damages § 147 (1935).
penalty, will obviously call for payment of an amount less than the contract price and will thus be more fair to the student than is the "Nebraska rule." Thus, since the formation of the terms of the contract are entirely within the control of the school, its remedy, were it to have the burden of proving the elements constituting its damages, is in its own hands.

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