

A. Introduction

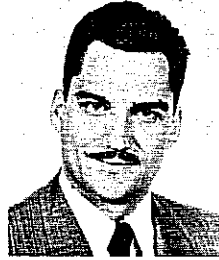
The commercial litigator is often confronted with clients who wish to assert a claim for lost anticipated profits of a business. When the business has no history of profitability, either because it is new or because the venture never reached fruition, the challenge of proving anticipated profits can be considerable. Because of the difficulty in proving such damages, Florida courts have expressed a reluctance, if not an absolute unwillingness, to award prospective profits to the new or unestablished business. However, the Supreme Court's recent decision in *W. W. Gay Mechanical Contractor, Inc. v. Wharfside Two, Ltd.*,¹ now allows the new or unestablished business to recover anticipated profits provided such profits can be proven with a reasonable certainty. The decision is a welcome and long overdue clarification of Florida's law concerning entitlement to lost profits.

B. Rule of Evidence or Per Se Rule: Uncertainty in Florida Case Law

Traditionally, the common law has denied recovery of lost profits to a new or unestablished business.² Courts have reasoned that in the absence of a history of earned profits, damages for anticipated profits are, as a matter of law, too speculative and uncertain to warrant recovery.³ More recent decisions have abrogated this "new business rule" and have permitted recovery where there is some method by which the anticipated profits can be established with reasonable certainty.⁴ Indeed, the majority of jurisdictions have now replaced the per se rule with a rule of evidence that permits recovery depending on the particular circumstances and methods of proof employed.⁵

The Florida Supreme Court took an early step in the direction of this majority trend in *Twyman v. Roell*.⁶ The suit in *Twyman* arose out of the profits lost by a partnership formed to improve and farm a tract of land. In the second year of the partnership, one of the partners failed to contribute his share of capital. As a result, the other partners were unable to plant English peas, which the partnership had agreed to market and sell. Other crops were planted late and sold at a reduced price. Subsequently, the partners brought suit against the nonperforming partner, seeking recovery of the profits anticipated from the sale of English peas. The trial court denied recovery, stating that prospective profits from the sale of crops never

Wharfside II: The Supreme Court Opens the Door to New Business for Recovery of Lost Profits



By Jeffrey S. Badgley

planted was too speculative and conjectural. The Supreme Court reversed, and stated the rule for prospective profits as follows:

The rule is well settled that if there is a yardstick or measure of damages by which prospective profits may be determined and they arise out of a contract in which profit is the inducement to its making they may be allowed if proven, whether they arise from farming, mechanical, or other contracts.

[I]f prospective profits from an elemental constituent of the contract, their loss, the natural result of its breach, and the amount can be established with reasonable certainty, such certainty as satisfied the mind of a prudent and impartial person, they are allowed. The requisite to their allowance is some standard, such as regular market values, or other established data, by reference to which the amount may be satisfactorily ascertained.⁷

The court observed that the plaintiffs had introduced evidence of the average yield of English peas, the cost of production, and the weather during the harvest season. The court found this evidence sufficient to justify an award for future profits, *despite the fact that the partnership had operated without a profit during the previous season.*

The *Twyman* court proscribed a rule of evidence to determine entitlement to prospective profits: a plaintiff was entitled to damages, regardless of its "track record," if it offered proof within a reasonable certainty to establish the amount of the anticipated profits. Nevertheless, Florida's district courts have consistently stated that new businesses are precluded from recovering anticipated profits, apparently adopting a *per se* rule.⁸ In so stating the rule, these cases cite to *New Amsterdam Casualty Co. v. Utility Battery Manufacturing Co.*,⁹ decided just one year before *Twyman*.

In *New Amsterdam*, the plaintiff, a battery manufacturing company, sued the defendant, its surety, for unwarranted appointment of a receivership. The plaintiff claimed that the surety's appointment of a receiver caused it damages in the form of lost profits during the period of receivership. The court denied recovery, stating:

It does not appear in this case that the plaintiff in the court below had ever made a profit from its business, nor was there any evidence of actual profits before or losses after the receivership, in such sort as that the court or jury might determine with any degree of certainty what profits had been lost as a result of the receivership proceedings.¹⁰

The *New Amsterdam* opinion did not state that evidence of past profits was a precondition for recovery. Rather, the court observed that a past performance "or facts of equivalent import, is usually required."¹¹ It seems clear that the court was applying a rule of evidence. There was, however, sufficient ambiguity in the court's opinion to cause lower courts to deny claims for anticipated profits of new or unestablished businesses for the next 44 years.

C. Wharfside Two: The Issue Is Resolved

This misapprehension of the *New Amsterdam* case did not daunt the plaintiff from asserting its claim for lost

profits in *Wharfside Two*. The plaintiff was a partnership formed to build and open a hotel. Shortly before opening, the hotel developed an odor problem that persisted for as long as three subsequent years. Complaints by guests resulted in reduced occupancy and a loss of profits to the partnership.

At trial, the partnership introduced into evidence several profitability studies. The reports were compiled before the construction of the hotel and showed profit projections based on similar hotel operations in the locality. However, the trial court refused to allow expert testimony comparing projected occupancy rates with those actually realized in order to establish the lost profit. Relying on previous district court opinions, the trial court ruled that because the hotel was a new business, the partnership was barred from seeking anticipated profits.¹²

On appeal, the first district recognized previous cases which denied recovery by new business of anticipated profits. It also observed, however, that a previous opinion of its own cited to *Tyman* as authority for entitlement to lost profits upon proof by reasonable certainty.¹³ Thus, it concluded that the trial court erred in refusing to admit the proffered evidence concerning the partnership's lost profit.

Wharfside Two provided the Supreme Court with a ripe opportunity to clarify its earlier decision in *New Amsterdam*. Noting the apparent conflict between *New Amsterdam* and *Tyman*, the court followed the reasoning of its less cited opinion and held that a business can recover lost prospective profits regardless of whether it has established a track record of earnings. However, the party seeking to recover must present "some standard by which the amount of damages may be adequately determined."¹⁴ The court, without elaborate comment, declared that the partnership's evidence was sufficient to provide such a standard to the jury. The case was remanded for a new trial.

D. Proving Lost Profits: The Claimant's Challenge

While *Wharfside Two* opens the door to new and unestablished businesses for recovery of anticipated profits, it remains to be seen how many claimants will successfully cross the threshold. Although it is now clear that entitlement to prospective profits is an issue of proof, precisely how those damages can be proven has been left to future cases.

The challenge of proving anticipated lost profits of a new or unestablished business inheres in the risk and uncertainty of any business venture. Nevertheless, most businessmen, like the plaintiffs in *Wharfside Two*, launch their venture with a modicum of informed assessment of that risk. Having assessed that risk, no prudent businessman would commit to a venture without a reasonable certainty of the likelihood and degree of profitability. When the venture becomes frustrated by actionable conduct, the task of the lawyer is to reconstruct his client's assessment in court to establish with a reasonable certainty the profits that would have been earned absent the actionable conduct. The practitioner will find some helpful suggestions from jurisdictions that have permitted recovery of lost profits by new businesses.

The "yardstick" method of calculating lost profits has a well established history of use in antitrust litigation.¹⁵ The yardstick method has been defined in the Eleventh Circuit as the "study of profits of business operations that are closely comparable to the plaintiff's."¹⁶ The claimant whose new or prospective business venture has been injured must identify a comparable firm (the "yardstick") in the same industry that has demonstrated a history of profitability.¹⁷ The yardstick business should, to prove the claimant's future profitability, be "as nearly identical to the plaintiff's as possible."¹⁸ Factors affecting comparability include product, market, capital structure, operations, and administrative policies. Studies of local markets or other markets comparable to the claimant's are particularly crucial for proving anticipated profits.¹⁹

Evidence showing the profitability of a predecessor business may be sufficient to establish a "yardstick." This evidence may be based on the claimant's prior experience in a similar business,²⁰ or in the operation by another party of the business that would have been successfully operated by the claimant absent the wrongful conduct.²¹ Conversely, the court may also consider subsequent business performance by the claimant, or a third party, as a sound basis for calculation of lost profits caused by delay in the operation of a new business.²²

Some courts have also shown a willingness to consider profitability projections based on reasonable and informed assumptions of future market behavior without the use of a "yardstick."²³ Industry averages may be utilized for showing the reasonableness of profitability pro-

jections.²⁴ While some courts may permit proof of lost profits based on the testimony of the injured party alone,²⁵ the claimant is well advised to employ the expertise of economists or accountants in projecting anticipated profits.²⁶ Courts are most likely to deny lost profits for future business performance where there are too many variables affecting profitability,²⁷ or where the analysis is unsupported by factual evidence.²⁸

The claimant may also borrow from methods employed in construction litigation. Damages incurred by the delay in completion of construction have traditionally been measured by the rental value of the completed structure for the period of delay or the reasonable return on the completed structure treated as an investment for the period of delay.²⁹ For calculation of lost profits, these figures may be adjusted by occupancy rates or other market conditions depending on the nature of the business.³⁰

Finally, the claimant should not be hesitant to use short "track records" of sales as evidence of future profitability. The courts have allowed base periods of three months,³¹ five months,³² six months,³³ and eight months³⁴ to establish the profitability of a business venture before the actionable conduct.

Conclusion

In the wake of *Wharfside Two*, Florida courts should now show a greater willingness to consider evidence of lost anticipated profits where there is some standard by which the amount of such damage may be adequately determined. The methods of proving lost anticipated damages will be as varied as the factual circumstances that give rise to the claims for which such recovery is sought. While this article suggests a few of the methods and techniques by which lost profits may be proven, the most valuable resource for the commercial litigator will be his own ingenuity and creativity, as well as the assistance and insight offered by expert consultants.

Footnotes

1. 545 So.2d 1348 (Fla. 1989).
2. See generally Dunn, *Recovery of Damages for Lost Profits*, 217 (3rd Ed. 1987).
3. See Knapp, *Commercial Damages, A Guide to Remedies in Business Litigation*, § 5.0B (1988).
4. See Knapp, *supra* ("In more recent years, courts have begun to avoid a per se rule. . .").
5. See Annot., *Recovery of Anticipated Lost Profits of New Businesses; Post 1965 Cases*, 55 ALR 4th 507, 508 (Majority of jurisdictions now allow recovery to new businesses if damages for

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Wharfside Two (continued from page 4)

lost profits can be established with reasonable certainty); *Ferrel v. Elrod*, 63 Tenn.App. 129, 469 S.W.2d 678 (1971) ("Each particular suit for anticipated profits must be decided upon its own particular facts. . . .").

6. 123 Fla. 2, 166 So. 215 (1936).
7. 166 So. at 217.

8. See, e.g., *Forest's Men's Shop v. Schmidt*, 536 So.2d 336 (Fla. 4th DCA 1988), *dismissed*, 542 So.2d 988 (Fla. 1989); *Pinberg v. Herald Fire Insurance Co.*, 455 So.2d 462, 464 (Fla. 3rd DCA 1984); *Polyglycoat Corp. v. Hirsch Distributors, Inc.*, 442 So.2d 958 (Fla. 4th DCA 1983), *rev. denied*, 451 So.2d 848 (Fla. 1984); *Wash-Bowl, Inc. v. Wroton*, 432 So.2d 766 (Fla. 2d DCA 1983); *American Motorcycle Institute v. Mitchell*, 380 So.2d 452 (Fla. 5th DCA 1980). *But see Williams v. Hardy*, 468 So.2d 429 (Fla. 5th DCA 1985) (Expert's estimate of ticket sales for performer-defendant's cancelled concert not too speculative to support jury's award of lost profits to concert promoter).

9. 122 Fla. 718, 166 So. 856 (1935).

10. 166 So. at 860.

11. *Id.*

12. *Wharfside Two, Ltd. v. W.W. Gay Mechanical Contractor, Inc.*, 523 So.2d 193, 195 (Fla. 1st DCA 1988), *aff'd*, 545 So.2d 1348 (Fla. 1989).

13. See *Massey-Ferguson, Inc. v. Santa Rosa Tractor Co.*, 415 So.2d 865 (Fla. 1st DCA 1982) (financial statements and sales projections sufficient to establish reasonably anticipated profits).

14. 545 So.2d at 1351.

15. See, e.g., *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 90 L.Ed. 652, 66 S.Ct. 574 (1946); *Rose Confections, Inc. v. Ambrosia Chocolate Co.*, 816 F.2d 381, 393-94 (8th Cir. 1987). See also Annot., *Measure and Elements of Damages Under USCS § 15 Entitling Person Injured in His Business or Property by Reason of Anything Forbidden in Federal Antitrust Laws to Recover Treble Damages*, 16 ALR Fed. 14, 45 (1973).

16. *Lehrman v. Gulf Oil Corp.*, 500 F.2d 659, 667 (5th Cir. 1974), *cert. denied*, 420 U.S. 929, 95 S.Ct. 1128, 43 L.Ed.2d 400 (1975) (antitrust action).

17. See *Home Placement Service, Inc. v. Providence Journal Co.*, 819 F.2d 1199 (1st Cir. 1987).

18. *Lehrman*, 500 F.2d at 667.

19. In *Home Placement Service v. Providence Journal Co.*, the plaintiff was denied lost profits due to its failure to produce evidence relating to comparability of the markets between its business and the purported "yardstick" business.

20. See *PRN of Denver, Inc. v. Arthur J. Gallagher & Co.*, 531 So.2d 1001 (Fla. 3rd DCA 1988); *Jayess Investments, Ltd. v. Barbee Foods, Inc.*, 155 So.2d 853 (Fla. 3rd DCA 1963), *cert. denied*, 161 So.2d 216 (Fla. 1964).

21. See *Malatesta v. Leichter*, 542 N.E.2d 768 (Ill.App. 1989) (prospective purchaser of automobile dealership received lost profits based on previous performance of seller);

Fishman v. Estate of Wirtz, 807 F.2d 547-48 (7th Cir. 1986) (antitrust action; unsuccessful bidder for professional basketball franchise recovered lost profits based on successful bidder's performance).

22. See *Cunningham v. Adams*, 808 F.2d 815 (11th Cir. 1987); *El Fredo Pizza, Inc. v. Roto-Flex Co.*, 199 Neb. 697, 261 N.W.2d 358 (1978); *Farrell v. Elrod*, 63 Tenn. 129, 469 S.W.2d 678 (1971); *Multivision Northwest, Inc. v. Jerrold Electronics Corp.*, 356 F.Supp. 207, 217, n.4 (N.D. Ga. 1972); *Lewis v. Mobile Oil Corp.*, 438 F.2d 500, 511 (8th Cir. 1971) (Arkansas law).

23. See *McDermott v. Middle East Carpet Co. Associated*, 811 F.2d 1422, 1426-28 (11th Cir. 1987); *Fields Engineering & Equipment, Inc. v. Cargil, Inc.*, 651 F.2d 589 (8th Cir. 1981); *Cardinal Consulting Co. v. Circo Resort, Inc.*, 297 N.W.2d 260 (Minn. 1980); *AutoWest, Inc. v. Peugeot*, 434 F.2d 556 (2nd Cir. 1970). See also *D&R Distributing Co., Inc. v. Chambers Corp.*, 608 F.Supp. 1290, 1307 (D.C. Cal. 1984) (lost profits in anti-trust litigation may be measured by any one of three ways: comparison, yardstick, and sales projections).

24. See *G. M. Brod & Co., Inc. v. U.S. Home Corp.*, 759 F.2d 1526 (11th Cir. 1985) (Expert used industry averages to support occupancy and rate projections for condominium/hotel development).

25. See *Miami International Realty Co. v. Paynter*, 841 F.2d 348, 351 (10th Cir. 1988) (applying Colorado law).

26. Some courts have required expert testimony to establish future profits. See *Larsen v. Walton Plywood Co.*, 390 P.2d 677, 687 (Wash. 1964).

27. See *Kenford Co., Inc. v. County of Erie*, 489 N.Y.S.2d 939 (A.D. 4th Dept. 1985) (Promoters of failed project for construction of stadium not entitled to recover lost profits on management contract).

28. See *Farm Crop Energy v. Old National Bank of Washington*, 750 P.2d 231 (Wash. 1980) (lost profits denied where expert's opinion of anticipated profits was not supported by sufficient factual basis).

29. See *Russo v. Heil Construction, Inc.*, 549 So.2d 676 (Fla. 5th DCA 1989). See also *Corbin on Contracts*, § 1029, 1092 (1964); *Restatement (Second) Contracts*, § 348 (1).

30. See *Quinn Blair Enterprises, Inc. v. Julien Construction Co.*, 597 P.2d 945 (1979) (owner recovered lost profits for contractor's delay in completing hotel, including damages resulting from loss of revenue to bar, restaurant, and associated facilities).

31. See *G. M. Brod & Co., Inc. v. U.S. Home Corp.*, 759 F.2d 1526, 1537 (11th Cir. 1985) (breach of contract for management of condominium/hotel development).

32. See *Heattransfer Corp. v. Volkswagenwerk, A.G.*, 553 F.2d 964, 983 (5th Cir. 1977), *cert. denied*, 434 U.S. 1087, 98 S.Ct. 1282, 55 L.Ed.2d 792 (1978) (antitrust action).

33. See *Manufacturing Research Corp. v. Greenlee Tool Co.*, 693 F.2d 1037, 1042 (11th Cir. 1982) (tortious interference with business relations).

34. See *Malcolm v. Marathon Oil Co.*, 642 F.2d 845 (5th Cir.), *cert. denied*, 454 U.S. 1125, 102 S.Ct. 975, 71 L.Ed.2d 113 (1981) (antitrust action). ■

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