A CASE FOR RECOVERY: DAMAGES FOR LOST PROFITS OF AN UNESTABLISHED BUSINESS

INTRODUCTION

The generally recognized rule is that an unestablished business cannot recover in a suit for lost profits. The rationale behind the "new business rule" was that the absence of income and experience renders proof of anticipated profits too speculative to meet the evidentiary standard of reasonable certainty when a new business is involved. 

2. The new business rule has been criticized, however, by those courts which have recognized that strict adherence to the rule could result in the denial of recovery despite the availability of sufficient evidence for determining probable losses. Thus, in recent years an increasing number of courts have been willing to allow recovery of lost profits of a new business if damages are shown with reasonable certainty.


Current developments in the recovery of lost profits can best be understood by an examination of the history of the new business rule, the confusion surrounding its application, and the modern trend toward rejection of the rule. In addition, this article will discuss the nature of the evidence available to prove lost profits of a new business in light of current evidentiary standards.

THE NEW BUSINESS RULE

The new business rule has its origins in the traditional reluctance of courts to allow any business to recover lost profits as damages. Although the rule has been considered well-established, there is widespread inconsistency in its application and its status. Recently, a trend has developed in decisions which have broken away from rigid adherence to the rule. These cases have either rejected the rule or refuse to consider it as an absolute bar to recovery.

In the past, anticipated profits of any commercial business, whether established or not, were considered too speculative to allow for recovery.5 Under the more rigid rules of evidence which applied at that time,6 lost profits were considered speculative and dependent on too many changing circumstances to warrant a judgment for their loss.7 However, courts have modified the rule that future profits could not be awarded because of their inherent uncertainty.8 This change may be partially attributed to the fact that the evidentiary standard of absolute certainty has been replaced by the more flexible standard of reasonable certainty.9 In addition, expert testimony and forecasting of future profits based on past records and market data have become increasingly accepted by the courts.10 Consequently, an exception developed which allowed

---

10. See Lost Profits as Contract Damages, supra note 6, at 1018-19.
for the recovery of lost profits of an established business. Under the exception, proof of actual damages was necessary before a court would allow recovery of anticipated profits. Lost profits of an established business are recoverable when: (1) it is reasonably certain that profits would have been realized except for the wrong; (2) such profits can be ascertained and measured with reasonable certainty; and (3) it is reasonable to suppose that such profits were within the contemplation of the parties, in the case of a contractual situation, or that the tortious conduct proximately caused the lost profits, in the case of a tort action.

In applying the above criteria, courts have generally considered profit history the most important factor in determining


12. See, e.g., cases cited in note 11 supra. In such cases recovery may often be based on opinion evidence from which inferences may be drawn that future profits were reasonably certain. Macke Co. v. Pizza of Gaithersburg, Inc., 259 Md. 479, —, 270 A.2d 645, 650 (1970); M & R Contr., Inc. v. Michael, 215 Md. 340, —, 138 A.2d 350, 354-55 (1958).

A judgment for actual damages is compensatory in nature, as the plaintiff is entitled to money as a substitution for a loss which may be measured in money. This compensatory award is contrasted with nominal damages, where money is awarded to vindicate a technical right when there has been no actual harm, and punitive damages which are primarily aimed at punishing the misconduct of the defendant. Neither nominal nor punitive damages are considered as substitution for actual losses suffered. D. Dobbs, Handbook on the Law of Remedies § 3.1, at 135 (1973).

Also in contrast to damages awards, which provide compensation for loss, are restitutionary awards, which deprive a defendant of his unjust gains rather than reimburse the plaintiff for his losses. Id. at 138.


These factors are based on the three distinct rules of damage assessment. The first rule requires that the plaintiff must show that the defendant's actions were the cause in fact of the damages. If the plaintiff had no loss or would have suffered the same loss even in the absence of the defendant's wrong, he is not entitled to recovery. D. Dobbs, supra note 12, at 148-49.

The second rule is that the plaintiff has the burden of proving the amount of damages suffered with reasonable certainty. If he is unable to show even a liberal estimate of the amount, he will be limited to nominal damages, if recoverable, or restitution. Id. at 148, 150.

Finally, under the third rule, damages must be denied if they are too remote. In contract cases, this means that damages must be within the "contemplation of the parties" at the time of contracting, in order for recovery to be allowed. Id. at 149. In tort cases, this rule is applied as the "proximate cause" test. If the damages asserted are not the kind against which the law was intended to protect, the court will state that the tort was not the "proximate cause" of the damages. Id. at 148.
whether profits would have been realized. Since usually only an established business is able to furnish records of past profits, courts have been reluctant to attempt to evaluate probable profits of a new enterprise. Any showing of anticipated profits of the new business has been considered as inherently too speculative to meet the evidentiary standard of reasonable certainty because there is no assurance that the business would have made such profits. This uncertainty of proving lost profits has given rise to the new business rule which bars recovery of lost profits of any new business.

Under the new business rule, a court must distinguish between claims for profits of an unestablished business and those of a well-established operation. If the business is classified as established, the bar on recovery of lost profits created by the new business rule can be avoided. A problem arises, however, because the courts are not consistent in determining what constitutes an established business.

In a few factual settings, the courts are generally consistent in their determination of whether a business is established. When a business is merely in contemplation rather than in actual operation, courts generally refuse to award lost profits damages because the business is deemed to be unestablished. Similarly, if a prod-

---


19. Compare Pace Corp. v. Jackson, 151 Tex. 173, —, 284 S.W.2d 340, 348-49 (1955) (cigarette wholesale business was considered "established" although it showed no profit during the six months of operation) with Atomic Fuel Extraction Corp. v. Estate of Slick, 386 S.W.2d 180, 189 (Tex. Ct. App. 1969) (uranium milling venture was not considered "established" when the venture had never made a profit during any year of its existence).

uct is not yet in the production or marketing stage, damages for lost profits may be denied. In both situations, determination of lost profits is considered too uncertain to allow for their recovery.

Once the new business has begun operation, however, it may be considered established, although it has not yet made a profit. In this situation, the circumstances which make a business established have been subject to several interpretations. In *Pace Corp. v. Jackson*, a newly formed cigarette business was considered established for the purpose of awarding damages although it had shown no profit and had been in operation only two months before the breach of contract occurred. In contrast, other courts have held that a business may be regarded as established only when it has been in operation long enough to give it permanency and recognition. In addition, some courts have required that the business have previously earned reasonably ascertainable profits. Thus, recovery of lost profits has been denied under the new business rule in the case of an operating business when the business had not shown a profit in any year.

Uncertainty in classification also occurs when a business which has been in successful operation changes into a different form or develops a new line of business. In these circumstances, the business may be considered new and damages for lost profits denied. One commentator has noted that some courts have permitted recovery for profits lost when an old business was prevented from expanding, although usually the added portion of the business is called a new venture and recovery has been denied. Similarly, when a business moves to a new location, it may be con-

---

24. 151 Tex. 179, 284 S.W.2d 340 (1955).
25. *Id.* at —, 284 S.W.2d at 348-49.
30. 64 HARV. L. REV. 317, 319 (1950). If the market demand is capable of proof, this result appears unreasonable, since the operation of the older part of the business should help to prove the efficiency of the management. *Id.* at 319-20.
sidered an unestablished business despite a past record of profits at a previous location.\(^{31}\) Thus, when an established business is prevented from moving to a different locale, anticipated profits from the new site may be denied under the new business rule.\(^{32}\) The same principle has been applied to bar recovery of anticipated lost profits of an established business which is acquired by new proprietors.\(^{33}\)

In addition to the uncertainty surrounding the issue of whether businesses are established, the status of the new business rule itself varies among jurisdictions. Courts appear divided as to whether the rule is a rule of law to be applied in all new business cases to bar recovery for lost profits or is merely a characterization of evidence as generally too speculative to allow recovery in a particular case. Thus, some courts which have propounded the new business rule support the principle as a well-established rule of law.\(^{34}\) Other courts have cautioned that the rule is not an absolute one, but, nevertheless, deny damages because the proof of profits of the new business is too speculative.\(^{35}\)

This confusion is illustrated by the holding of the court in *Evergreen Amusement Corp. v. Milstead*,\(^{36}\) and the interpretation of this case by subsequent courts. In *Evergreen*, the court denied lost profits to a newly constructed drive-in theater whose opening had been delayed until after the peak summer period by the contractor's breach.\(^{37}\) The court refused to consider evidence, including expert opinion, which supported the loss of profits.\(^{38}\) The only recovery permitted was the rental value of the property since lost profits of the new business were determined to be too speculative in nature.\(^{39}\) The court emphasized that it would not lay down a "flat rule," however, it noted that no case had permitted recovery of profits of a new business under comparable circumstances.\(^{40}\) Thus, the court applied the rationale behind the rule without de-


\(^{35}\) *E.g.*, Evergreen Amusement Corp. v. Milstead, 206 Md. 610, —, 112 A.2d 901, 905 (1955).

\(^{36}\) 206 Md. 610, 112 A.2d 901 (1955).

\(^{37}\) *Id.* at —, 112 A.2d at 904.

\(^{38}\) *Id.*

\(^{39}\) *Id.* at —, 112 A.2d at 906.

\(^{40}\) *Id.* at —, 112 A.2d at 905.
DAMAGES FOR LOST PROFITS

claring an absolute bar to recovery in cases involving new businesses. Despite the fact that the decision in *Evergreen* did not espouse a "flat rule," it has often been cited as supporting the absolute rule that no new business can recover lost profits.\(^{41}\)

In spite of the confused and somewhat inconsistent application of the new business rule, it is still followed in a number of jurisdictions.\(^{42}\) A modern trend away from the rule has appeared, however, in the opinions of courts which refuse to consider the rule an absolute bar to recovery.\(^{43}\) A growing number of courts support the principle that if a new business can present proof of the existence of lost profits, that evidence should be considered by the trier of fact. These courts have stated that recovery for lost profits should not be denied merely because a business is new if factual data is available to furnish a basis for the prediction of anticipated losses.\(^{44}\) Given sufficient evidence of the appropriate business type, location, and personnel, courts may find that the chance of success for a new business outweighs the chance of failure.\(^{45}\) Some courts argue that it should be permissible, although difficult, in fact to prove that a new business would have earned profits.\(^{46}\) In these jurisdictions, the newness of the source of anticipated profits is not itself a bar to recovery if such profits were within the contemplation of the parties and their amount is satisfactorily proved.\(^{47}\)

Among those courts which have allowed a new business to re-


cover lost profits, some have been willing to completely abandon or disregard the new business rule. The vestiges of the rule still remain, however, in other decisions which have allowed recovery of lost profits of an unestablished business. The necessity for a clear reversal of the old rule has been obviated simply by deciding not to apply it as a "hard and fast" rule. Thus, the absolute rule of law which excluded proof of lost profits has been increasingly replaced by a rule of evidence which admits the proof of lost profits.

PROOF OF LOST PROFITS DAMAGES

If a court chooses to abandon or relax the new business rule, the crucial issue becomes whether the lost profits have been proven with reasonable certainty. In such jurisdictions, loss of


Attempts to circumvent the rule without reversing it have led to the juxtaposition of seemingly contradictory holdings within a single decision. One court, for example, conceded that it had recognized the general rule that lost profits of a new business were too speculative to recover but concluded that while the law recognized that it was more difficult to prove lost profits of a new business, the law did not hold that it might not be done. Leoni v. Bemis, — Minn. —, 255 N.W.2d 824, 826 (1977). Damages for lost profits were thus allowed by the court without expressly reversing the new business rule. Such decisions ultimately lead to the same result as those which abandoned the rule, but they take a more circuitous route.

50. Dunn, supra note 1, at 434. There is authority for the position that the term "speculative profits" is not actually a classification of profits but is instead a characterization of the evidence that is introduced to prove that they would have been made but for the defendant's action. Fera v. Village Plaza, Inc., 396 Mich. 639, —, 242 N.W.2d 372, 373-74 (1976); 5 A. CORBIN, CORBIN ON CONTRACTS § 1022, at 139 (1964).


To satisfy the reasonable certainty standard, the "best evidence" available must be produced to show a fair prospect of success and the income which would have followed. E.g., Vickers v. Wichita State Univ., 213 Kan. 812, —, 518 P.2d 512, 517 (1974); Jaffe v. Alliance Metal Co., 337 Pa. 449, —, 12 A.2d 13, 14 (1940); Reefer Queen Co. v. Marine Constr. & Design Co., 85 Wash. 2d 774, —, 440 P.2d 448, 452 (1968); 5 A. CORBIN, supra note 50, at 143 n.90. Dean McCormick, in describing the best evidence rule, stated that, "if [the claimant] has furnished the most satisfactory data that the particular situation admits of this suffices" on questions of certainty of proof. C. McCormick, supra note 14, at 110. The problem of certainty involves questions of admissibility of items of proof and sufficiency of items to make a case for the jury. Id. at 107. The court should not require more information than businessmen commonly utilize. Lost Profits as Contract Damages, supra note 6, at 1018.
DAMAGES FOR LOST PROFITS

prospective profits may be recovered if the evidence establishes with reasonable certainty both the occurrence of lost profits and the extent of damage.\(^5\) To recover, the new business must also establish causation.\(^5\) Thus, the elements which must be proven in order to recover profits of an established venture should be applied to show the anticipated profits of an unestablished business.\(^5\) In determining whether the reasonable certainty standard has been met the court considers both the nature of the business involved and the type of evidence presented.

In considering the nature of the business\(^5\) it has been recognized that courts have treated the profits in particular types of businesses as inherently too speculative to support any recovery.\(^5\) The stability of the industry as a whole, not merely that of the new

---


The law requires only that evidence not be so uncertain as to afford no reasonable basis for inference, leaving damages to be determined by sympathy and feeling alone. \(^5\) E.g., Fera v. Village Plaza, Inc., 396 Mich. 639, —, 242 N.W.2d 372, 374 (1976); \(^5\) A. CORBIN, supra note 50, at 139. The general rationale is that the wrongdoer should be the party to bear the risk of uncertainty that his wrong has created. \(^5\) E.g., Biegel v. RKO Radio Pictures, Inc., 327 U.S. 251, 265 (1946); C. MCCORMICK, supra note 14, at 102; Lost Profits as Contract Damages, supra note 6, at 1003. See For Children, Inc., v. Graphics Int'l, Inc., 352 F. Supp. 1280, 1284 (S.D.N.Y. 1972); Ferrell v. Elrod, 63 Tenn. App. 129, —, 469 S.W.2d 678, 686 (1971).


\(^54\) \(^5\) See, e.g., El Fredo Pizza, Inc. v. Roto-Flex Oven Co., 199 Neb. 697, 705, 261 N.W.2d 358, 363-64 (1978). For the characteristics which must be shown to recover profits of an established business, see note 13 and accompanying text supra.\(^5\)

\(^55\) \(^5\) E.g., Frank Sullivan Co. v. Midwest Sheet Metal Works, 335 F.2d 33, 41 (8th Cir. 1964) (applying Minnesota law).

\(^56\) \(^5\) Lost Profits as Contract Damages, supra note 6, at 1013-14; 64 HARV. L. REV. 317, 320 (1950).
business, may exert a strong influence on the result.\textsuperscript{57} If the nature of the business is intrinsically speculative, even the best evidence will likely prove inadequate to establish a reasonable certainty of lost profits.\textsuperscript{58}

Cases involving the development of mineral resources appear to bear out the importance of the nature of the business' setting in a court's determination that lost profits have been established with reasonable certainty. In this situation, the speculative nature of the business may render the proof of profits uncertain.\textsuperscript{59} In the recent case of \textit{Fisher v. Hampton},\textsuperscript{60} which dealt with the anticipated profits of a proposed oil-drilling venture, the court departed from the new business rule in announcing that new businesses could recover lost profits.\textsuperscript{61} The obstacle in the path of recovery however, was the lack of evidence that any oil could have been recovered at a profit from the aborted operation.\textsuperscript{62} In \textit{Fisher}, evidence was presented which suggested that "'[t]here's no guarantee that any well will produce, no matter where you drill,' 'All oil drilling is a speculative venture, a high risk venture.'"\textsuperscript{63} This case illustrates the difficulties which plaintiffs may face in proving the existence of lost profits in a speculative industry.

Other businesses whose profits are considered too speculative to satisfy the reasonable certainty standard are those in the fields of entertainment and liquor sales.\textsuperscript{64} One commentator has noted that in these fields, regardless of the statistics presented as to the particular new business in question, the whole industry has been considered by courts as too subject to the whim of the public to free any award from the stigma of uncertainty.\textsuperscript{65} However, the speculative nature of the industry has not barred recovery in all

\textsuperscript{57} 64 HARV. L. REV. 317, 320 (1950).
\textsuperscript{58} See, e.g., Baumer v. Franklin County Distilling Co., 135 F.2d 384, 387, 390 (6th Cir. 1943) (although liquor distributor was experienced in business, had a history of profit, and the product had a good sales record, whiskey sales intrinsically too speculative to permit recovery); Todd v. Keene, 167 Mass. 154, 45 N.E. 81 (1896) (recovery denied even though actor of high repute had drawn large audiences to the same theater during recent performance, since theater profits are too speculative and variable).
\textsuperscript{60} 44 Cal. App. 3d 741, 118 Cal. Rptr. 811 (1975).
\textsuperscript{61} Id. at 748, 118 Cal. Rptr. at 815.
\textsuperscript{62} Id. at 748-49, 118 Cal. Rptr. at 815-16.
\textsuperscript{63} Id. at 749, 118 Cal. Rptr. at 816.
\textsuperscript{64} Baumer v. Franklin County Distilling Co., 135 F.2d 384, 390 (6th Cir. 1943); Evergreen Amusement Corp. v. Milstead, 206 Md. 610, —, 112 A.2d 901, 905-06 (1955); 64 HARV. L. REV. 317, 320 (1950).
\textsuperscript{65} 64 HARV. L. REV. 317, 320 (1950).
cases. For example, in *Exton Drive-In, Inc. v. Home Indemnity Co.*, it was suggested that a new drive-in theater would be permitted to recover losses from a delay in completion if the resulting damages were sufficiently certain to permit recovery. Similarly, in *Gerwin v. Southeastern California Association of Seventh Day Adventists*, a case involving lost profits of a cocktail lounge, the court held that although the business may be new, loss of prospective profits may be recovered if proven with reasonable certainty. Despite the dicta in these cases, recovery was denied in both due to lack of sufficient evidence. From *Exton* and *Gerwin*, it can be inferred that proving lost profits in the entertainment and liquor industries may be difficult because of their dependence on public whim.

In contrast to the liquor and entertainment industries cases are decisions in which litigation involved the television and communications industries. In *Vickers v. Wichita State University*, the court held that the new business, which was formed to produce regional college basketball telecasts, could use evidence based on television and advertising industry experience to establish proof of lost profits. The court decided that the televising of conference games and the selling of advertising connected with the telecasts was not a new or untried business, and, therefore, profits could be calculated with reasonable certainty.

Other businesses whose profits may be deemed inherently uncertain are those whose character or product is new to a particular area. The uncertainty in this situation would stem from its uniqueness to the locality and the resultant difficulty in predicting success in a new market. Proof of lost profits, however, may meet the standard of reasonable certainty if based on the business'
successes in markets encompassing large geographical areas rather than on experiences in small localized markets.\textsuperscript{77} For example, lost profits were held recoverable in a case involving a type of disposal plant which had never been built or operated in the United States.\textsuperscript{78} The court held that since the plant in question had been operated in France, there would be a sufficient basis from which to compute profits if proven.\textsuperscript{79}

If the business involved is part of a network of similar businesses, a history of profitability in an established chain operation may eliminate the problem of speculation associated with the profits of untried enterprises. Accordingly, in these cases courts have appeared less reluctant to award lost profits.\textsuperscript{80} This may be attributed to the fact that successful franchises are considered very stable, reporting success rates of eighty percent, much higher than those found in small new businesses in general.\textsuperscript{81}

In recent litigation, one court\textsuperscript{82} allowed a new business within a chain operation to recover lost profits under Uniform Commercial Code Section 2-715.\textsuperscript{83} Under section 2-715(2)(a), lost profits arising from a seller's breach are recoverable as consequential damages.\textsuperscript{84} The court in \textit{El Fredo Pizza, Inc. v. Roto-Flex Oven Co.}\textsuperscript{85} examined a situation in which owners of a new pizza parlor sued for profits allegedly lost when an oven failed to function as warranted.\textsuperscript{86} In awarding damages, the court considered the his-


\textsuperscript{79} Id. at 167.


\textsuperscript{81} V. STEFFLRE, SMALL NEW BUSINESS (1st ed. 1961). The success rates are based on a comparison of businesses which continued operation with those which failed.


\textsuperscript{83} NEB. REV. STAT. (U.C.C.) § 2-715 (Reissue 1971). Section 2-715(2)(a) provides: "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 contacting had reason to know and which could not reasonably be prevented by cover or otherwise." Id.

\textsuperscript{84} E.g., Lewis v. Mobil Oil Corp., 438 F.2d 500, 510-11 (8th Cir. 1971); National Farmers Org., Inc. v. McCook Feed & Supply Co., 196 Neb. 424, 243 N.W.2d 335 (1976).

\textsuperscript{85} 199 Neb. 627, 261 N.W.2d 358 (1978).

\textsuperscript{86} Id. at 698, 261 N.W.2d at 360.
In a case arising from a tort claim brought by a franchise, the court in *Smith Development Corp. v. Bilow Enterprises, Inc.*, considered an attempt to keep "McDonald's Golden Arches" from building at a particular location. It concluded that evidence of profits at other McDonald's locations established profits for the particular franchise with reasonable certainty. In contrast, the court in *Mullen v. Brantley,* refused to consider profits lost when a Shakey's Pizza Parlor was prevented from opening in close proximity to another Shakey's franchise. The record of profits obtained from three franchised pizza parlors and the nationwide chain as a whole were not regarded as presenting any reasonable basis for judgment of profits. The court based its decision on the new business rule, contending that there were too many contingencies upon which to fix the measure of damages. However, the major emphasis was placed on testimony that when parlors had been located in close proximity to one another, financial failure occurred. The evidence would have proved inadequate to establish lost profits under an evidentiary standard of reasonable certainty, without relying on the new business rule. Thus, these cases illustrate the importance of the existence of other franchises in proving lost profits with reasonable certainty.

Once a court has determined that a particular business or type
of business is sufficiently stable so as to remove the possibility of lost profits from the realm of mere speculation, the court must examine the nature of the evidence presented. Evidence which is proffered must contain sufficient factual data from which the occurrence of lost profit damages may be determined with a reasonable degree of certainty. In considering the nature of the evidence, courts should not exclude the types of information commonly used by businessmen in reaching business decisions.97

A history of profitability, if available, may be used to establish lost profit damages.98 A new business which continues in operation may be able to produce records for a comparable period of time.99 In Vogue v. Shopping Centers, Inc.,100 the Michigan Supreme Court reversed an appellate court decision which had denied recovery of lost profits to a clothing store which had experienced a seventeen-day delay in opening.101 The appellate court found the evidence presented at trial insufficient to permit recovery as a matter of law.102 The supreme court determined that lost profits calculated by using the history of sales for a time period equal to that of the delay could establish lost profits with reasonable certainty.103

Consequently, the fact that a business has remained in operation can be significant in determining the existence of lost profits, especially when records show the business operating both during and after the defendant’s action.104 As rules of admissibility have been relaxed, business records have gained increasing acceptance in the courts.105 If the profits are shown in this manner with rea-

97. Lost Profits as Contract Damages, supra note 6, at 1018.
102. 58 Mich. App. at —, 228 N.W.2d at 406-07.
104. See, e.g., El Fredo Pizza, Inc. v. Roto-Flex Oven Co., 199 Neb. 697, 707-08, 261 N.W.2d 358, 364 (1978); Pace Corp. v. Jackson, 151 Tex. 179, —, 284 S.W.2d 340, 344-45 (1965). But see Evergreen Amusement Corp. v. Milstead, 206 Md. 610, —, 112 A.2d 901, 904 (1955). Similar factual data may be used to determine lost profits for a business actually established and operated for a period, although it may later be forced to discontinue. See Pace Corp. v. Jackson, 151 Tex. 179, —, 284 S.W.2d 340, 344-45 (1965).
105. Lost Profits as Contract Damages, supra note 6, at 1018, wherein the author
sonable certainty, by actual experience, there is no reason to pe-
nalize the new business by denying recovery for lost profits. Thus, business records can remove some uncertainty from calculations of lost profits for a new business.

However, since a new business may have no record of profits, it is much more difficult for the new venture to establish with sufficient certainty a claim of lost profits. A new business without an immediate predecessor and without a record of profits to provide a sufficient basis for an award of damages may have to show that the market demand was such that the business would be sure to receive all the orders it was able to handle.

Proof of demand for a particular business within a given locale may be shown by market surveys and forecasting techniques. The business world often uses predictions of future demand made by market analysis based on studies of samplings of consumer demand and preference. As commercial usage of these forms of analysis become widespread, there is likely to be increased judicial recognition of the admissibility and reliability of such evidence.

Another manner of showing demand is to establish that the new firm had substantial orders or was operating in an area of scarce supply. When it can be proved with reasonable certainty that the new business could have sold all materials it had, it may not be necessary to show firm orders. An acute shortage in the market as a whole can be sufficient to show a demand for the product. On the other hand, when there has been no evidence offered of any orders or any contracts for sale of the business' notes that objections to such records on hearsay grounds have been displaced by recognition of their importance in proving the effects of commercial transactions. 

108. Id. There still remains the question of whether the business can efficiently process all the orders it receives. Id.
109. Lost Profits as Contract Damages, supra note 6, at 1018-19.
product, recovery of lost profits may be denied.\textsuperscript{114}

Prompt public acceptance, once the new business is begun, can provide proof of demand which may remove the speculative character of future business profits.\textsuperscript{115} In a decision involving a McDonald's hamburger franchise, America's acceptance of the McDonald-type merchandising showed that profits would have been certain.\textsuperscript{116} In another case, testimony which showed the "great enthusiasm [of] all persons concerned" about a product has been regarded as important in showing that the sale of the product would have been profitable.\textsuperscript{117}

Proof of loss of customer goodwill, like proof of demand, may provide evidence of the existence of lost profits.\textsuperscript{118} However, loss of customer goodwill, in comparison to demand, may be difficult to ascertain in the case of new businesses.\textsuperscript{119} In \textit{El Fredo Pizza, Inc. v. Roto-Flex Oven Co.}\textsuperscript{120} the defendants had supplied the pizza parlor with a defective oven which allegedly caused uneven baking of pizzas.\textsuperscript{121} Proof of loss of goodwill was supplied by some evidence that customers were dissatisfied with pizza baked in the defective oven.\textsuperscript{122} Considering such evidence "scanty at best," the court failed to find sufficient evidence of lost profits due to decreased sales attributed to the failure of customers to return.\textsuperscript{123} In \textit{Jorgensen v. Tesmer Manufacturing Co.},\textsuperscript{124} the court denied damages to a farm implement dealer who had been supplied with materials not fit to be incorporated into a tiller.\textsuperscript{125} The court emphasized that the dealer had not produced any witnesses who could testify that sales had been lost due to customers' experiences with the defective tiller.\textsuperscript{126} In attempting to prove loss of

120. 199 Neb. 697, 261 N.W.2d 358 (1978).
121. \textit{Id.} at 700, 261 N.W.2d at 361.
122. \textit{Id.} at 711, 261 N.W.2d at 366.
123. \textit{Id.}
125. \textit{Id.} at —, 459 P.2d at 535.
126. \textit{Id.} at —, 459 P.2d at 538. \textit{See} 64 HARV. L. REV. 317, 318 (1950). The new business owner may attempt to prove his losses by the direct testimony of customers
customer goodwill, the inability to locate potential customers who have been deterred from purchasing can be an insurmountable barrier to the new businessman.

As an alternative method of proving lost profit damages, evidence of operating profits of comparable businesses may be produced to meet the standard of reasonable certainty. If such evidence is available, the entrepreneur might attempt to show profits of similar businesses during the period for which recovery is sought. A number of courts have appeared willing to consider evidence of profits of similar businesses in the vicinity. The fact that the new business owner does not present proof of the operating history of comparable businesses in the same locality may enable a court to conclude that the evidence fails to satisfy the test of reasonable certainty. Similarly, in the case of franchise operations, the history of experiences of other members of the chain may remove damages from the area of speculation.

Some courts have considered the previous business experience of the new business owner as relevant in determining whether to award damages. The expertise gained by the businessman in his dealings in the commercial world is likely to increase the chances of success of the new venture. Profits are considered within the realm of certainty when the prime mover is an "old hand" in the business. An old hand may include an accomplished salesman or one with prior business experience in the same industry.

In addition, expert opinion may provide evidence of profits which meets the test of reasonable certainty. The best evidence

who would have patronized him, but as a result of the defendant's wrong did not. However, where such customers are unknown, this method is unavailable to the owner. Id.


132. See C. MCCORMICK, supra note 14, at 108.


requirement becomes a reasonable rule of necessity when expert opinion is the best evidence available.135 Reasonable methods of estimation may be made with the aid of this opinion evidence.136 Experts should be competent to testify as long as their opinions afford a reasonable basis for inferring whether lost profits exist.137

Expert testimony alone may be sufficient to establish lost profits of a new business.138 The weight to be given the expert's testimony is for the trier of fact to determine.139 However, there must be facts sufficient upon which to base the expert's opinion in order for it to be admissible.140 As the science of analyzing business costs and market behavior matures, the use of expert witnesses to help with problems of proof is likely to increase.141

An expert in the field need not have a scientific, economic, or mathematical background.142 Expert witnesses may be persons in active management of the same or comparable businesses who possess a background in the industry, including personal experience.143 Officers of the new business corporation may be well-qualified as experts by reason of trade experiences.144 The plaintiff himself may have sufficient experience in the business so that an award may be based on his testimony alone.145 When the business involves the sale of more than one type of product, experts in the marketing of each type may be used. In a case involving a combined liquor and bookstore business, the court admitted the testimony of experts in the liquor business, bookstore business and representatives of liquor distributors in the area.146 Similarly, a geologist's opinion may constitute proof that there is no indication

136. Id.
137. Id.
138. Id.
141. Lost Profits as Contract Damages, supra note 6, at 1019.
142. Compare the notes after Fed. R. Evid. 702, which state: "The fields of knowledge which may be drawn upon are not limited merely to 'scientific' and 'technical' but extend to all 'specialized' knowledge. Similarly the expert is viewed, not in a narrow sense, but as a person qualified by 'knowledge, skill, experience, training or education.'" Fed. R. Evid. 702 (Advisory Committee Notes).
that any oil or minerals could have been recovered. An accountant making assumptions as to how much a salesman could sell may be allowed to draw conclusions about what prospective profits should be. If an accountant testifies that the new business showed no profit, the court may consider the opinion as sufficient proof to conclude that there is no basis for awarding damages. Management consultants may also qualify as experts. One court, in determining that lost profits were uncertain in the operation of a new disposal plant, suggested that if a garbage expert had testified as to the exact nature of the city's garbage, damages might have been allowed.

Once the court has found sufficient evidence that lost profits do exist, the court must then examine the evidence presented in order to determine the amount of damages. Those courts which have abandoned rigid adherence to the new business rule have generally agreed that while uncertainty as to whether any damages were sustained at all is fatal to recovery, uncertainty as to amount is not. All that is required is that there is some rational basis from which the court and jury can estimate damages.

---

152. Lost Profits As Contract Damages, supra note 6, at 1027. The type of damages allowed depends on what the evidence has established with reasonable certainty. While evidence may be insufficient to prove the existence of lost profits from decreased revenue, lost profits due to increased labor costs may be allowed. El Fredo Pizza, Inc. v. Roto-Flex Oven Co., 199 Neb. 697, 711, 261 N.W.2d 358, 366 (1978). The problem of determining an exact amount lies in the nature of the lost profits themselves. The profits are not the subtraction of existing wealth; rather, they constitute the prevention of hoped-for gain. 5 A. Corbin, supra note 50, at 139.
Each case should be approached in an individual and pragmatic manner, and each claimant should be required to furnish the best proof available as to amount of loss. Absolute mathematical certainty in fixing an exact amount is not required. If the court is reasonably certain of the existence of lost profits, it will permit the jury to award damages even when the amount is supported by little evidence. When the question of profits is submitted to the jury, the jury has a great deal of discretion in determining the amount of the verdict.

If the business has continued to operate, an estimation of total profits may be shown based on future income measured by using the history of sales during the period immediately following their delay. Actual operation of the same business at a profit for an equal period, even though at a later date, may allow calculation of profits with a reasonable degree of certainty. In this case, it is assumed that the profits are what the party would have made earlier except for the wrong. Economists can estimate the amount of lost profits by showing the profit experience of an average business during its lifetime and plotting the rate of earning profits at

When substantial orders have been made, profits can be predicted with some certainty. Accordingly, judging by the number of orders, an anticipated sales percentage can be estimated. Thus, the businessman will be entitled to the gross profits on such sales less the expenses chargeable to the project.\textsuperscript{163}

In determining the amount of profits it is also necessary for the plaintiff to prove his costs of operation. This is important because it is generally considered that when loss of anticipated profits is an element of damages, it means net and not gross profits.\textsuperscript{164} This is particularly true in the case of new businesses which have not gone into operation, since it would be error to award gross profits when the business had never incurred any overhead expenses.\textsuperscript{165}

Since expenses or costs must be subtracted from anticipated profits, any formula of proving damages will require proof of costs as well as income.\textsuperscript{166} Proof of cost may be almost as difficult as proof of future income.\textsuperscript{167} Cost may be proven by expert opinion evidence and by cost records which accurately reflect operating expenses.\textsuperscript{168} In \textit{Itvenus, Inc. v. Poultry, Inc.},\textsuperscript{169} the court refused to determine if the new business rule was in effect.\textsuperscript{170} It decided, however, that even if it was not, the new business could not re-

\begin{footnotesize}
\textsuperscript{162} Id. at 1030 n.203.
\textsuperscript{165} Gross profits are the excess of the price received over price paid for goods before deductions are made for the cost of operation. Hill v. City of Richmond, 181 Va. 744, —, S.E.2d 48, 54 (1943). Net profits are considered gains made from sales after deducting the value of labor, materials, rent and all expenses together with the interest of capital employed. Gerwin v. Southeastern Cal. Ass'n of Seventh Day Adventists, 14 Cal. App. 3d 209, 223, 92 Cal. Rptr. 111, 119-20 (1971).
\textsuperscript{166} See Covington Bros. v. Valley Plastering, Inc., — Nev. —, —, 566 P.2d 814, 818 (1977). Examples of overhead include officers' salaries, depreciation, interest and office rent. Id. at 117.
\textsuperscript{167} Evidence of the amount of lost profits should include a computation of both income and costs. In unsuccessful cases, both elements of the total profits equation were not covered by the evidence. E.g., Burks v. Sinclair Ref. Co., 183 F.2d 239, 242 (3d Cir. 1950); \textit{Lost Profits as Contracts Damages, supra} note 6, at 996, 1027. In cases involving contracts, profits may be ascertained by showing total cost and expenses, including labor, and then deducting that sum from the contract price. The result is profit. Innkeepers Int'l, Inc. v. McCoy Motels, Ltd., 324 So. 2d 676, 679 (Fla. Dist. Ct. App. 1975).
\textsuperscript{168} \textit{Lost Profits as Contract Damages, supra} note 6, at 997. In addition to the cost of goods themselves, there are other costs to be considered such as costs of delivery, merchandising, advertising and operation. \textit{Id.}
\textsuperscript{169} Id. at 1028.
\textsuperscript{169} 258 So. 2d 478 (Fla. Dist. Ct. App. 1972).
\textsuperscript{170} Id. at 482.
\end{footnotesize}
cover where the record failed to show "any substantial competent" evidence of overhead costs or operating expenses which could have been charged against anticipated profits.\(^{171}\) In *Burk v. Sinclair Refining Co.*,\(^{172}\) the court rejected the rule that since the gas station involved was a new business, prospective profits would be speculative.\(^{173}\) However, the court placed emphasis on the fact that there was no testimony as to the cost of operation.\(^{174}\) While the jury was charged concerning the operation costs to be deducted, it did not have sufficient evidence to arrive at an approximation of net profits on estimated gasoline sales.\(^{175}\) The station owner was therefore not permitted to recover lost profits until such costs were established.\(^{176}\)

Once the plaintiff has established both that profits would have existed except for the wrong and that such profits can be measured with reasonable certainty, it must be shown that such profits were within the contemplation of the parties, in a contractual situation, or proximately caused by the wrong, in the case of a tort action.\(^{177}\) It must be shown that the interference with plaintiff's profits is a probable result of defendant's wrong.\(^{178}\) Additionally, evidence rebutting an inference of other causative forces should be offered by the new business plaintiff.\(^{179}\) The court may refuse to use a comparable time period to measure profits, when the business has continued operation, if the defendant's wrong is not established as the only factor contributing to lost profits.\(^{180}\) One method to avoid this obstacle would be to apportion damages according to the percent of loss of profits estimated to be caused by the defendant's wrongful conduct.\(^{181}\) This approach would prevent the plaintiff from being completely denied any recovery no matter how large a factor the defendant's conduct was in causing loss of profits.\(^{182}\)

\(^{171}\) *Id.*

\(^{172}\) 183 F.2d 239 (3d Cir. 1950).

\(^{173}\) *Id.* at 242.

\(^{174}\) *Id.*

\(^{175}\) *Id.*

\(^{176}\) *Id.* at 242, 244.

\(^{177}\) *E.g.,* Cranston Print Works Co. v. Public Serv. Co., 291 F.2d 638, 649 (4th Cir. 1961); J.H. Horne & Sons Co. v. Bath Fibre Co., 272 F.2d 8, 11 (1st Cir. 1959). *See cases cited in note 13 supra.*

\(^{178}\) 64 Harv. L. Rev. 317, 319 (1950). Expert testimony may be needed to show the causal link but often the relationship is obvious. *Id.*

\(^{179}\) *Id.*


\(^{181}\) *See* C. McCormick, *supra* note 14, at 109-10.

\(^{182}\) *See id.* The author states that some courts "will allow the jury to make the apportionment [among causative forces] unless the defendant clears up the uncertainty." *Id.* at 110; Bigelow v. RKO Radio Pictures, Inc., 327 U.S. 251, 265 (1946).
CONCLUSION

Although the general rule is that lost profits of an unestablished business are not recoverable, there appears to be an increasing number of courts willing to allow a new business to recover lost profits. Given the right conditions of appropriate business, location, and personnel, the chances of success for a new business may outweigh the chance of failure.\textsuperscript{183} In determining whether a new business should recover damages, courts have accepted the same standard used for determining the lost profits of an established business—that of reasonable certainty. Thus, a rule of law has been replaced by a rule of evidence. The rule of evidence appears to be preferable,\textsuperscript{184} since it is impossible to foresee all the possible situations in which valid claims for lost profits could be asserted although the business had not begun operations.\textsuperscript{185}

Once courts consider that both established and new businesses should be governed by the standard of reasonable certainty, they should not require appreciably more evidence to prove lost profits of the new business. The evidence necessary to establish profits should depend on the individual circumstances. Courts should only require the best proof available, not absolute certainty, in estimating profits. If factual data such as profits of a new business that continues, or of a comparable business, are furnished by proof, then that evidence should be admitted regardless of whether the business is established.\textsuperscript{186} Experts should be allowed to interpret such data by giving an opinion based on knowledge or experience. Once the existence of lost profits is established with reasonable certainty, uncertainty as to the exact amount of profits should not be fatal to recovery. The wrongdoer, not the new business owner, should bear the risk of uncertainty that his own wrong has created.

No business is free from uncertainty. If courts search only for hazards which might deprive a particular venture of profits, no injured plaintiff could ever recover for damages. Strict adherence to the "new business" rule can result in denial of damages where jus-

\textsuperscript{183} C. McCormick, \textit{supra} note 14, at 108.
\textsuperscript{184} Dunn, \textit{supra} note 1, at 434.
\textsuperscript{185} Id.
\textsuperscript{186} In Larsen v. Walton Plywood Co., 65 Wash. 2d 1, 390 P.2d 677 (1964), the court concluded that the reasons behind the new business rule vanish when the analysis of market conditions and a profit showing of similar businesses operating under substantially the same conditions is made. \textit{Id.} at —, 390 P.2d at 687.
tice should require otherwise. As courts come to realize the significance of anticipated gains in a commercial society and the increasing reliability of economic data, the general tone of their decisions can be expected to become more liberal. However, the multiplicity of contributing factors involved still makes it difficult to forecast with precision what degree of certainty will be considered reasonable by a particular court. Each particular suit should be decided on its own peculiar facts within the broad general rules laid down in prior decisions. When a new business can provide proof of lost profits, it should be allowed to make its case.

*Karilyn E. Kober—'80*

---