Conflict in the Measure of Contract Damages: Cost of Performance (Replacement) Versus Difference in Value (Indemnity)

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INTRODUCTION

The fundamental rule with regard to damages given to an innocent party upon the breach of his contract by a defaulting party was laid down by Lord Atkinson in the case of Wertheim v. Chicoutimi Pulp Co.:

And it is the general intention of the law that, in giving damages for breach of contract, the party complaining should, so far as it can be done by money, be placed in the same position as he would have been in if the contract had been performed ... That is a ruling principle. It is a just principle.1

However, in trying to follow this rule, the courts have sometimes been faced with the issue of a conflict in the measure of damages; this conflict comes about by the problems raised by the following two considerations of Lord Atkinson's rule:

1. Exactly what position would the complaining party have occupied if the contract had been performed?
2. Just how far can the court go in awarding monetary compensation?

A conflict in the measure of damages often arises in building contract cases in the following manner. A contracts with B to have B build a house for A. The specifications are clearly defined in the contract. A refuses to pay for the house and B brings an action for the contract price. A claims a reduction in the amount that it will take to alter or repair the house to conform exactly with the specifications. B claims that A's reduction is simply the difference in value between the house A contracted for and the house A received. These two measures are referred to as the cost of performance (or replacement) and the difference in value (or indemnity) respectively.

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The conflict also arises in "lost chance" or "speculative damages" situations. For example, M is a racetrack operator who sponsors a $150,000 race. N enters his horse in a field of 8 horses, but then M decides he only wants to race 7 horses and he scratches N's entry. N argues that his horse probably would have won and he is entitled to substantial damages.

Another field in which the conflict appears is in oil or gas "test well" cases. Take the situation where X has a lease on land and Y is a well-driller. X contracts with Y to give Y a half-interest in any minerals discovered if Y will drill a test well. Y defaults and X sues for the cost of drilling. X claims that the only loss Y suffered is the difference in value between the land before the contract was to be performed and after the contract was performed and that this difference is negligible.

These problems do not arise often, but when they do the end result often is confusion smothered with judicial jargon. The building contract cases have been cluttered with confusing jargon for over a century and the exploratory work cases have been without rationale ever since a very misleading judgment twenty years ago. However, in recent years, the Courts have begun to grapple with the issues and have laid down realistic and defined approaches. The culmination of this problem of a conflict in the measure of damages has recently resulted in an extremely substantial award of over $350,000 in Dolly Varden Mines Ltd. (N.P.L.) v. Sunshine Exploration Ltd. et al.\(^2\)

However, in order to best appreciate the problem, it is essential to retrace the development of the law back many years.

PART I

The Basis of the Problem — the Early Building Contract Cases and Their Development

Although the English courts had to face the problem of a conflict in the measure of damages as early as 1855,\(^a\) the problem was first squarely faced in 1882 in the case of Wigsell v. School for Indigent Blind.\(^4\) In that case, the plaintiffs sued for damages for the defendant's breach of its covenant to erect a wall around part of its land, which it had bought from the plaintiffs, adjacent to the plaintiffs' land. The defendant did not build the wall. The cost of building the wall would have exceeded the diminution in the value of the plaintiffs' land caused by the defendant's default. The plaintiffs did not build the wall but sought to recover the cost of erecting the wall as damages. It was held that the proper measure of damages was not the cost of erecting the wall, but the monetary difference between the value of the plaintiff's land upon the breach of the contract and what the value would have been had the contract been performed. In considering the motives of the plaintiffs in not bringing an action in the Court of Chancery for specific performance, Field


\(^a\)Pell v. Shearman (1855), 10 Ex. 766, 156 E.R. 560.

\(^4\)(1882), 8 Q.B.D. 357.
Osgoode Hall Law Journal, touched upon the real issues behind the court's analysis of the problem:

But it was also open to the plaintiffs to do what they have done, viz., bring this action for damages, in which event they will be under no obligation whatever to expend the amount recovered in erecting the wall, and most probably would never think for a moment of any such expenditure, which to us, at least, would seem a simple waste of the money. 6

Thus, Field, J. really went beneath the superficial contract and he considered its true rationale — did the parties contract for a simple sale of land or for a sale of land with an understanding that it was absolutely essential that the wall be built? Or, were the plaintiffs unconcerned about the wall but merely seeking a windfall recovery in the form of damages measured by the high cost of performance? How certain can the court be that the aggrieved party will have the contract performed if and when he is awarded the cost of performance? And, most important, by granting such expensive relief, would the courts not be pursuing a policy which would, in effect, be “a simple waste of money”?

The first Canadian case dealing with this type of conflict in the measure of damages was Wood v. Stringer. 6 The work in question was the building of a church; the last of the work completed was the pews. As the pews were being put in, objection was made to their material and workmanship. To replace the inferior materials would have cost $185, whereas the difference in value between the bad materials and the better materials which should have been put in was estimated at only $25. In this case, however, the owners spent $35 for repairs themselves. In assessing the Master's award of only $25 for the difference in value, Boyd, C. said:

That allowance can hardly be deemed an adequate measure of the set-off or deduction to which the proprietors are entitled. 7

He then stated that the owners were entitled to have deducted from the contract price at least the $35 for repairs and the $25 for inferior materials. If either party objected the matter was to go back to the Master on a reference.

The case seems to suggest that once it can honestly be said that the owners did contract for the work to be done in a certain manner and that this manner was essentially what the innocent party bargained for (as exemplified in this case by the fact that the owners took it upon themselves to repair the poor work), then the court will award more than the difference in value between the work contracted for and the work received. Moreover, the fact that the owners had taken action subsequent to the breach to have the pews built in a particular manner prompted the judge to allow the higher damages.

However, the first Canadian judge to really pierce the issue and to develop a sound reason or policy for awarding the cost of performance was Wetmore, J. in two cases which he decided in the Northwest Territories. In the second of these cases, Allen v. Pierce, 8 he applied the principles which he himself had enunciated in the earlier case of Clarke v. Lee. 9 The Allen case

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6 Id. at 363-364.
6 (1890), 20 O.R. 148 (Ch.Div.).
7 Id. at 152.
8 (1895), 3 Terr.L.R. 319.
9 (1893), 3 Terr. L.R. 191.
was an action on a building contract brought by the contractor against the owner to recover the balance of the contract price. However, the evidence was that the work had not been done in the manner for which the parties had contracted. Wetmore, J., in dealing with the issue of damages available to the owner, explored the underlying issue of just what the basis of the contract was:

[It is not a mere matter of difference between the value of the material supplied and that contracted for, or of the work done and that which ought to have been built under the contract. If these were the standards of damages there would be no point in a man contracting for the best materials; he might as well contract at the start for an inferior quality, because they are cheaper. The owner of the building is, therefore, entitled to recover such damages, or to have such deductions made as will put him in a position to have just the building he contracted for.]

Thus, the correct measure of damages was the sum which it would take to put the owner in such a position as to have the building altered so as to make it in accordance with the contract. Certainly this award meets the expectation interest of the innocent party.

Thus, Wetmore, J. set out a further policy consideration for awarding the expectation interest and for recognizing the reliance of the innocent party. If the measure of damages is simply the difference in value between the building as contracted for and built, then the owner has wasted his time in contracting for good materials and good workmanship — any builder would be able to deliver poor quality and workmanship and still be paid. Moreover, if the quality of the building is not that for which the owner contracted, he is faced with the situation whereby he must accept and pay for a building for which he did not contract and which he does not want. The owner must be able to get the cost of performance if he has made it clear that his intentions and expectations were to contract not for any building, but for a building of a certain specified quality.

The underlying idea of determining exactly what the innocent party bargained for and what he reasonably could expect was a major consideration in the case of M. J. O'Brien Ltd. v. Freedman.

The facts of the case were as follows. In a written contract for a sale by the plaintiffs and purchase by the defendant of buildings which had become useless to the plaintiffs and which they wished to have removed from their land, there was no express undertaking by the defendant to remove the buildings, but in the written agreement a definite time was set aside for that purpose. The defendant paid the consideration-money and entered and removed part of the buildings but left the foundations. The plaintiffs claimed that the correct measure of damages was the $10,000 cost of placing them
in the same position as if the contract had been performed (i.e. the cost of performance); however, the defendant contended that the plaintiffs were only entitled to the $1,000 cost of the depreciation of the value of the land. The trial judge awarded damages based on the cost of performance. However, in the Court of Appeal, the award was based on the difference in value. One of the reasons why the Court of Appeal reduced the award was because they found on the contract that the defendant was not under an express obligation to remove the foundations. Therefore, the opinions expressed on the issue of the measure of damages are largely obiter; however, Ferguson, J.A. stated that even if there had been an express obligation on the part of the defendant to remove the foundations, a determining factor in arriving at the correct measure would be a consideration of the benefits which each party could reasonably be expected to derive from the performance:

[It may be that, if the defendant expressly, and without doubt, undertook to remove these foundations, and it appeared that the contract was entered into for some special purpose, or to acquire some benefit or fancied benefit which the plaintiffs sought to get, the Court should and would direct specific performance of such a contract; but, where it appears that there was no special reason for making a contract to remove the foundations ... and that the cost of removal is out of all proportion to any benefit, real or fanciful, that the plaintiffs could get from the performance of the obligation, and that damages is an adequate remedy, the trial judge was not, I think, required ... to award as damages the expense or cost of performing the work contracted to be done. His duty was, I think, to award the plaintiffs, as pecuniary compensation and damages, the difference pecuniarily estimated between what the plaintiffs' position would have been if the contract had been fulfilled and their existing position.]

The underlying reasons for the importance of the benefit argument are threefold. First, there is the problem previously mentioned with regard to the Wiggell case — by granting the cost of performance the Court may be giving a windfall to the innocent party, if the benefit of the contract was not known by the defaulting party. Secondly, unless such expected benefit could reasonably have been made known to the defaulting party, how can the Court hold that party to the higher measure of damages and at the same time insist that contract damages are not punitive? And, thirdly, will the Court not, in some cases, be encouraging economic waste if the measure of damages is the higher cost of performance?

Thus, in considering the problem of whether or not to award the cost of performance as the measure of damages, the courts, in these early building contract cases, have seen fit to explore the following questions:

1. Was the part of the contract which was not performed an essential part for which the innocent party really bargained?
2. Was the innocent party's intention clearly known by the defaulting party?
3. Will the innocent party get a windfall if he is given the higher award?
4. Can it reasonably be said that the innocent party will, indeed, have this necessary construction completed?

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12 Id. at 465-466.
13 (1882), 8 Q.B.D. 357; See discussion pp. 180-181, supra.
14 The leading case in the United States on this point is Jacob & Youngs v. Kent, 230 N.Y. 239, 129 N.E. 889, 23 A.L.R. 1429 (1921), where Cardozo, J. refused to grant the cost of performance because it was out of proportion to the good to be attained.
Will the courts encourage economic waste if the higher award is given? What real benefit would have accrued to the innocent party if the contract had been performed? That is, is the benefit expected just an increase in the value of the land or is it some special benefit which the innocent party could only get by contracting expressly for it?

PART II

The "Lost Chance" or "Speculative Damages" Problem

Another area of damages in which the courts have been faced with the difficult problem of having to decide on conflicting measures of damages is that of "speculative" or "lost chance" damages. This area is often discussed under the topics of remoteness and quantum (nominal vs. substantial damages); however, conflicts in the measure of damages often arise in "lost chance" or "speculative damages" cases.

One of the leading authorities in this area is the English case of Chaplin v. Hicks. In that case, the Court of Appeal affirmed a judgment awarding £100 to the plaintiff for her loss of a chance to win a prize. The defendant had selected the plaintiff as one of fifty people chosen from a group of six thousand entrants; of the fifty, twelve were to be further selected and offered theatrical engagements. The defendant failed to give the plaintiff a reasonable opportunity of being interviewed in accordance with the advertised rules.

The Court of Appeal, in upholding the award for substantial, rather than nominal, damages was confronted with a conflict in the measure of damages appropriate in such a "lost chance" case. There is a breach of contract; however, there is little or no reliance placed on the contract by the innocent party. Damages (expectation) must flow from the breach — yet is the proper compensation the higher award arrived at by assuming that the entrant would be selected and thereby giving her the monetary equivalent of the reward, or is it the lower award arrived at by assuming that the entrant would not be selected and thereby giving her nothing?

Two principles adopted in the case suggest that the Court is really intent on punishing the wrongdoer and on giving the innocent party substantial monetary compensation for the lost chance on which she might reasonably have relied. First, the Court expounded the old principle that the fact that damages cannot be assessed with certainty does not relieve the wrongdoer of paying damages for his wrong. Secondly, the Court agreed that the jury's award should be upheld, even if the amount of their verdict was really a matter of guesswork. Considering the normal requirement that damages must be proven, these two points certainly bear out the probability that the Court will not allow a wrongdoer to breach a contract without having to pay for his breach.

The headnote of the case, often quoted in subsequent cases, seems to suggest that a deprived entrant, in order to collect substantial damages, must show that he would have been a member of a select and limited group; however, the important point to note is that substantial, and not nominal, damages are available on the basis of a "lost chance":

Where by contract a man has a right to belong to a limited class of competitors for a prize, a breach of that contract by reason of which he is prevented from continuing a member of the class and is thereby deprived of all chance of obtaining the prize is a breach in respect of which he may be entitled to recover substantial, and not merely nominal, damages.16

The Chaplin case was considered in a case before the British Columbia Court of Appeal, McGee v. Clarke.17 In that case, the defendant obtained from the plaintiff a transfer of the plaintiff's unexplored mineral claim under an agreement to pay her $1000 as soon as he should sell it; the defendant also agreed to keep up the assessment work in the meantime. He allowed the claim to lapse for default in assessment work and it was lost as it was re-staked by another.

Comparing the instant case with the Chaplin case, MacDonald, C.J.A. said that the present case was "a very much stronger case, a case of the deprivation of the plaintiff of her mineral claim by default on the defendant's part."18

In assessing damages, Galliher, J.A. rejected the plaintiff's claim for the $1000 mentioned in the agreement. The Court held that the proper measure of damages should be the value of the property the plaintiff lost by reason of the defendant's breach of the contract. Since the plaintiff could offer no significant evidence of the value of the property, damages of only $50 were awarded.

In speaking of the value of the property, MacDonald, C.J.A. said:

An unexplored mineral claim is of speculative value. Its value can only be determined by what it will bring in the speculative market. Its real value cannot be ascertained except by the expenditure of money in exploitation.19

Several points are worth noting here. First, it seems that the court places the onus on the innocent party to prove the worth of his land. In view of the facts that both parties agreed to pay $1000 in the event of a sale and that the intention of the parties was for the possible sale, why should the totally innocent party be burdened with the onus?20 Secondly, the plaintiff received absolutely no benefits from the contract while the defendant received the transfer of the mineral claim and possible value if minerals were discovered or if sale was completed. Certainly the court took little effort to compensate the plaintiff for her three losses — loss of possible sale, loss of mineral rights, and loss of alternate contract with another party. And if the measure of damages is the value of the lost property, why shouldn't these other three losses be taken into consideration in evaluating

16 Id. at 786.
18 Id. at 594, 38 B.C.R. at 158.
19 Id.
20 The burden of proof problem has been considered in "oil test well" cases in the United States. See W.O. Roberts Jr., Damages — Measure of Damages for Breach of Contract to Drill Oil or Gas Wells (1956), 13 Wash. & Lee L. Rev. 207.
the worth of the property? It seems that the Court, in assessing damages, lost sight of the basic principles of reasonable foreseeability and intention of the parties.

An earlier case in which the Saskatchewan Court of Appeal took a more realistic approach to a similar problem was *McGee v. Rosetown Electric Light and Power Co. Ltd.*\(^{21}\) A contract for the sinking of a well provided that if no water were obtained after a specified depth the contractor was to receive a certain remuneration per foot sunk, but if water were obtained at the said or a lesser depth the contractor was to be remunerated at a higher rate. The contractor was compelled by the default of the other party to discontinue the work.

Brown, J., in dealing with the measure of damages, made quite clear his position that the innocent party should get the benefit of the higher award:

> There is no way, apart from the actual process of sinking the well, of ascertaining what might have happened. The defendants, by their action in refusing to carry out the contract, have placed the plaintiff in the position where he is deprived of the privilege of making the test.\(^{22}\)

> In considering the contractual intention of the parties, he continued,

> As it was quite possible within the contemplation of the parties that the plaintiff would have sunk the well 500 feet, and at that depth secured the necessary flow of water, and as that is the possibility most favourable from the plaintiff's point of view, I am of opinion that his damages should be assessed on that basis.\(^{23}\)

The measure of damages seems quite appropriate: both parties intended and contracted to drill to the specified depth and there was a reasonable chance that water would be found. It is not unreasonable for the defendant to expect that the plaintiff's benefit from the contract might have been the speculation or the chance that water would be found. Why should the Court not give the innocent well-driller compensation for his lost part of the bargain — the speculation or chance? However, the difficulty in determining the value of a "lost chance" seems to have influenced the Court in awarding damages as if the chance had been realized.

Another important case on the question of speculative damages is *Carson v. Willitts.*\(^{24}\) Here the plaintiff entered into a contract with the defendant whereby, in consideration of a share in certain rights which the plaintiff had acquired, the defendant undertook to bore three wells in order to explore a certain territory for oil. The defendant bored one well and then refused to bore the other two. The plaintiff's claim for damages caused the court to consider whether nominal or substantial damages should be awarded.

Masten, J.A. considered the damages that the plaintiff should be awarded:

> In my opinion, what the plaintiff lost by the refusal of the defendant to bore two more wells was a sporting or gambling chance that valuable oil or gas would be

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\(^{22}\) *Id.* at 555.

\(^{23}\) *Id.* at 556.

found when the two further wells were bored. If the wells had been bored and no oil or gas of value had been found, the effect would be that the plaintiff has lost nothing by the refusal of the defendant to go on boring. On the other hand, if valuable oil or gas had been discovered, by the boring of these two wells, he has lost substantially. It may not be easy to compute what that chance was worth to the plaintiff but the difficulty in estimating the quantum is no reason for refusing to award any damages.25

He then directed that the plaintiff was entitled to recover for the loss of the chance that valuable oil or gas might have been discovered.

The decision has been questioned, and rightly so, in subsequent cases.26 The loss is not as serious as was the loss in McGee v. Clarke27 where time was of the essence or as in McGee v. Rosetown Electric28 where the contractor lost his chance of speculation; here, the plaintiff owner made no effort to seek substitute performance or to mitigate his damages. Damages on the usual basis of the difference between the contract price and the market price of drilling could have been awarded without taking away the plaintiff's loss of chance.

The one point overlooked by the Court in Carson v. Willitts and which could have distinguished that case from the other cases is the problem of evidence. In Carson there was no evidence that any oil would have been found if the other two wells had been drilled. In fact, the evidence was, if anything, unfavourable from the plaintiff's point of view since the one well which had been bored revealed nothing. However, in Chaplin v. Hicks29 there was evidence adduced to show that the plaintiff had a one-in-four chance of success. The Court there considered that this constituted evidence equivalent of a "reasonable probability of the plaintiff's being a prize-winner."30

Therefore, if more than nominal damages are to be awarded in a case of "lost chance" or "speculative damages", it is essential that the claimant adduce sufficient evidence to show that he had a reasonably probable chance of success in his venture. It was this consideration of sufficiency of evidence which prompted the Supreme Court of Canada to explain Chaplin and to criticize Carson in the case of Kinkel v. Hyman.31 In the latter case the defendants were directors of a company and held stock of a second company in trust for their shareholders. They sold this stock to the plaintiff without first having obtained the consent of their shareholders. The plaintiff

25 Id. at 458, [1930] 4 D.L.R. at 980.
26 See, e.g., Kinkel v. Hyman, [1939], 4 D.L.R. 1 at 7, [1939] S.C.R. 364 at 386, where Crocket, J., discusses the Carson case and states that substantial damages should not have been awarded in that case.
See also Kranz v. McCutcheon (1920) 19 O.W.N. 161 (Ont.C.A.), where the defendant drilled only two out of five wells which he had contracted to drill. The evidence was that the general reputation of the oil field had declined because of the first two failures. The trial judge directed a reference on the basis of substantial damages as the proper award. The Court of Appeal varied this direction by striking out the words "substantial damages" and substituting the words "the damages, if any, sustained."
29 [1911] 2 K.B. 786 (C.A.).
30 Id. per Fletcher Moulton, L.J., at 795.
then resold a large proportion of the stock to the defendant directors in return for a 9 month's option to repurchase a portion of them providing that the defendants obtained ratification of the first transaction by 51% of their shareholders at a general meeting. The defendants did not call a meeting within the 9 month period of the option. The plaintiff brought an action for breach of contract.

It was held by the Supreme Court of Canada that there was a breach of contract. However, the Court allowed only nominal damages because the plaintiff could offer no evidence upon which a finding could be made that there was a reasonable probability that a general meeting of the shareholders would have approved the first transaction, and that the option would have been of real monetary value. In considering the Chaplin and Carson cases, Crocket, J., gave this explanation:

For my part I can find no authority in either Chaplin v. Hicks or Carson v. Willitts justifying any Court in awarding any more than a nominal sum as damages for the loss of a mere chance of possible benefit except upon evidence proving that there was some reasonable probability of plaintiff realizing therefrom an advantage of some real substantial monetary value.32

On the basis of the above reasoning, Crocket, J. stated that substantial damages should not have been awarded in the Carson case and that they should not be awarded in the case before him.

In summary, the Kinkel case has somewhat clarified the approach which Canadian courts take in "lost chance" or "speculative damages" cases. The following points must be noted:

1. if there is not a reasonable opportunity for the aggrieved party to seek alternate performance or if he is a member of a select group of persons, then the Court will award substantial damages;

2. evidence must be adduced to show that the claimant lost a reasonable probability of realizing an advantage of some real substantial monetary value;

3. the Courts will do whatever possible to see that the innocent party gets the benefit of the doubt of the outcome of the speculation in order to thereby award substantial damages.

However, it is this third point, although pervasive throughout the cases, that the Courts often hide behind their judgments. Perhaps a new class of damages called "reasonably hopeful expectation" should be considered!

PART III

The "Failure to Drill" Problem — The Cotter Case and its Misapplications

Closely related to the "speculative damages" problem is the problem which arises when a party has failed to drill a well or to do development

32 Id. at 7, [1939] S.C.R. at 386.
work as promised in a contract.\(^{33}\) The turning point of these cases came with the Supreme Court of Canada decision in 1950 in Cotter v. General Petrol- 
eums Ltd. and Superior Oils Ltd.\(^{34}\) However, in order to best evaluate the 
decision in the Cotter case, it is essential to study the earlier case of Cunningham v. Insinger,\(^{35}\) a case which was quickly distinguished in Cotter.

In the Cunningham case, the respondent mine owner gave the appellant mine operator an option to purchase an operating mine. When the first instalment payment fell due, the operator procured from the owner an extension of time for payment upon the condition that the operator do certain development work consisting of tunnelling which had not been mentioned in the original option. The operator failed to make the required payments and he relinquished possession of the mine and surrendered his option without having done the work. The owner sued for damages amounting to the cost of the work. The trial Judge gave judgment for the owner directing a reference to ascertain the quantum of damages for all tunnelling work not done by the operator, thus determining that the proper measure of damages was the cost of the work to the owner which the operator had failed to perform. This judgment was affirmed in the British Columbia Court of Appeal; in the Supreme Court of Canada the measure of damages became the major issue.

Duff and Anglin, JJ. dealt with the question of damages and held that in the circumstances of this particular case the cost of doing the work was the proper measure. Chief Justice Davies and Mignault, J., while concurring in the result, did not deal with the issue of damages and Idington, J. dissented. Duff, J. after referring to the argument of counsel that the plaintiff is entitled to recover, and only entitled to recover, the pecuniary value of the advantage he would have obtained by a performance of the contract which would, in this case, be the equivalent of any increase in the value of the mine to arise therefrom said:

Cases may no doubt arise in which the test suggested by [Counsel's] argument would be the only proper test, and difficult and intricate as the inquiry might be, it would be the duty of the Court to enter upon an examination of the effect of doing the work upon the value of the property.

On the other hand, cases must arise in which the plaintiff's right is plainly to recover at least the cost of doing the work. If it were conclusively made out, for example, that the work to be done formed part and a necessary part of some plan of exploration or development requisite, from the miner's point of view, for developing the property as a working mine, and necessary, from the point of view of businesslike management, so that it might fairly be presumed that in the event of the option lapsing the owner would in the ordinary course have the work completed, then the damages arising in the ordinary course would include the cost of doing the work and would accordingly be recoverable under the rule.

In the case before us I think no serious difficulty arises. The letters appear to afford abundant evidence that both parties were proceeding upon the footing that this work was necessary in the course of developing the mine according to the

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\(^{33}\) Although this problem has already been touched upon in the previous discussion of the case of Carson v. Willitts (1930), 65 O.L.R. 456; [1930] 4 D.L.R. 977 (Ont.C.A.). I will dismiss that case since the decision has been practically overruled by Kinkel v. Hyman [1939], 4 D.L.R. 1, S.C.R. 364. See also Kranz v. McCutcheon (1920), 19 O.W.N. 161 (Ont. C.A.). For a recent article covering this field alone, see M. Sychuk, Damages for Breach of an Express Drilling Covenant (1970), 8 Alta.L.Rev. 250.


owner’s plans and it is upon the basis of that being accepted as a fact, I think, that the trial Judge proceeded.\(^\text{36}\)

And in holding as he did, Duff, J. was clearly of the view that he was applying in a special way the general rule relating to assessment of damages:

As already intimated, however, I am not disposed to base my decision upon any supposed rule of law other than the general rule to which reference has been made. Having regard to the manner in which the case was conducted in the Courts of British Columbia, I think the proper application of the general rule is that which I have indicated above.\(^\text{37}\)

Anglin, J. also stated that this was a special case in which the cost of performance should be awarded:

It is a fair inference not only that the plaintiff regards the work as essential but that it is work which he will have done. It is probably necessary to reach that conclusion in order to justify the departure made by the trial Judge from the ordinary rule that the measure of damages for breach by a defendant of a contract to perform work on the plaintiff’s land is the actual pecuniary loss sustained by the plaintiff as a result of such breach, i.e., the difference between what would have been the value of the premises had the work contracted for been done and their value with it unperformed.\(^\text{38}\)

These judgments make it clear that no special rule is applied to decide whether or not the measure of damages will be the cost of performance. The general rule awarding the expectation interest is departed from or applied in a special way only to this effect: if a finding can be made that the work agreed to be done forms a part of a scheme or plan, the execution of which the owner regards as essential to the proper development of the property, and if it can be fairly presumed that the owner intends in any event to carry out the work, then the damages may include the cost of the performance of the work.

The rule seems simple enough. However, does not the rule really say what I have been proposing all along — i.e., the Courts will award the cost of performance if performance is essentially what the innocent party bargained for? Isn’t this approach really the same approach which the Courts have taken in the building contracts cases and the speculative damages cases? The Courts seem to be asking whether the contract was simply for some general development work or for some special work which, if not performed as specified, would disrupt the larger benefit or plan. Perhaps the “benefits” approach can be explained in terms of the “necessary part of some plan ... for developing the property”\(^\text{39}\) in Duff, J.’s terminology. Here there is, beyond any doubt, a measure of awarding the reliance interest. Although the breach of the contract may have involved only the digging of a tunnel, the success of the larger plan of development was largely dependent on this one tunnel. And the owner reasonably could rely on the contract to the effect that the tunnel would be dug. If the Courts simply award damages on the normal scale, the owner does not get what he bargained for, nor does he get compensation for his reasonable reliance. Furthermore, the Court (per Duff and Anglin, JJ, in this case) seems to decide if the work was essential on the basis of whether or not it is likely that the owner will have the work done


\(^{37}\) Id. at 438, [1924] S.C.R. at 15.

\(^{38}\) Id. at 439, [1924] S.C.R. at 16.

\(^{39}\) Id. at 437, [1924] S.C.R. at 14.
in any event. This test, however, is as old as the Wigsell case which I discussed earlier. The Courts simply do not want to give uneconomic damages or windfall awards in the form of damages measured by the cost of performance to a party who is not likely to have the work done at all.

The Cunningham test seems easy enough to apply. However, when the Cunningham case came to be applied some twenty-six years later, the case was distinguished. This was in the famous case of Cotter v. General Petroleums Ltd. and Superior Oil Ltd., a case in which the judgments of the Supreme Court of Canada are so ambiguous that it has taken at least one wrongly decided case and nearly twenty years to straighten out the issue of the proper measure of damages. However, we shall discuss those problems later on.

In the Cotter case the owner of petroleum and natural gas under certain Alberta lands granted an option on the resources. Clause 2 provided the option would be exercised within a specified time by the optionees erecting the necessary machinery on the lands and commencing the drilling of a well. Clause 3 contained a covenant by the optionees to exercise the option in the time specified by clause 2, and provided that, upon failure to do so, the optionor would be entitled to exercise any remedies for breach of the covenant despite the lapse of the option. It was agreed by the parties that the covenant was given as consideration for the granting of the option. McLaurin J., in the trial Court, held first, that there was a binding obligation on the optionee to drill a well and, secondly, that the proper measure of damages for the failure to do so was the $53,500 it would cost to drill. An appeal to the Alberta Supreme Court was allowed, but on the ground of repugnancy in the documents; the case then came before the Supreme Court of Canada. The Court allowed the appeal on the question of damages fixing them in the amount of $1,000. Kerwin, J., with whom Rinfret, C.J.C. agreed, held that upon a proper consideration of the documents there was no obligation on the optionees to drill a well at all, and, while he agreed that the plaintiff should have more than nominal damages, he reduced them to $1,000. On the question of damages he said,

Notwithstanding that the appellant's case was put as if the respondents' covenant was to dig a well, which as I have indicated is not in my view its proper construction, the appellant is entitled to more than nominal damages. The proper measure is not the cost of performance to the respondents but the value of performance to the appellant: Erie County Natural Gas & Fuel Co. v. Carroll, [1911] A.C. 105. Adapting Lord Atkinson's language at the foot of p. 118, it was the appellant's business to show the damages and he cannot be permitted to recover damages on guesswork or surmise.

Locke, I. dissented from the result without dealing with the question of damages and Cartwright, J., with whom Fauteux, J., agreed, held that there was a clear obligation on the optionees to drill a well and awarded damages

40 See, discussion supra.
43 See, discussion infra.
45 Id.
in the amount of $1,000. After approving the statement by Lord Atkinson in Wertheim v. Chicoutimi Pulp Co., Cartwright J. continued:

What further benefits would have resulted to the appellant from the performance of the contract? If the respondents had drilled the well to the prescribed depth and it had proved a producer, the appellant would have received, (a) his share of the proceeds, and, (b) the benefit of having the head lease validated, by the performance of the lessee's covenant to drill, not only as to the 80 acres described in the sublease but as to the whole 160 acres described in the head lease. If on the other hand, as, from the evidence of the geologists, would seem much more probable, the well had proved a failure the appellant would not have received benefit (a) but would have received benefit (b). It must be remembered, however, that as a result of the respondents' breach the appellant holds the whole 160 acres free from any claim of the respondents. No part of the consideration which under the contract would have passed to the respondents has passed, except that from April 21, 1948 until some time in June, 1948, when they repudiated the agreement, the respondents had rights in the 80 acres and the appellant was not free to deal therewith. Under these circumstances, I do not think that the cost of drilling is the proper measure of damages. Suppose that instead of the consideration set out in the contract the appellant had agreed to pay the respondents $53,500 to drill the well and the respondents had repudiated the contract before the date set for the commencement of the work and before any monies had been paid to them. In such a case by analogy to the rule in the case of building contracts the measure of damages would seem to be the difference (if any) between the price of the work agreed upon and the cost to which the appellant was actually put in its completion. I think it will be found that those cases in which it has been held that the cost of drilling is the proper measure of damages are cases where the consideration to be given for the drilling had actually passed to the defendant. Examples of such cases are Cunningham v. Insinger, [1924] 2 D.L.R. 433, [1924] S.C.R. 8, and Pell v. Shearman (1855), 10 Exch. 766, 156 E.R. 650 (a contract to sink a shaft).

Thus, while Kerwin, J. and Rinfret, C.J.C. based their judgments on the finding that there was no obligation to drill, and, therefore, the rule in Cunningham v. Insinger could not apply, Cartwright and Fauteux, J.J. distinguished the Cunningham case upon the basis that in the case at hand no part of the consideration for the drilling had actually passed to the defendant. They distinguished those cases in which the measure of damages was held to be the cost of the drilling upon the ground that they were cases in which consideration had entirely passed. Cartwright, J. held in the particular circumstances of the Cotter case that the measure of damages was the difference between the value to the owner of the consideration that he had agreed to give for drilling the well, and the value to him of the consideration, which acting reasonably he would have to give to have the well drilled by others, and there was no evidence on the value of this consideration.

This line of reasoning has done nothing to clarify the problem of the conflict in the measure of damages — the Cunningham decision can be easily interpreted in terms of economic benefit and the essential basis of the bargain. However, by introducing the idea of the sufficiency of consideration, Cartwright, J. has departed from the rule that the Courts will not consider adequacy of consideration and has done nothing other than hide the real issue. Certainly here, as in most of the other cases, the problem is simply the question of what the parties really bargained for, and whether or not the part of the contract to do work really went to the essence of the bargain. Cartwright, J. could have applied the Cunningham test in this manner:

although the drilling constituted the total plan of exploration or development, the plaintiff, by his conduct, has shown that he would not have had the work completed in the ordinary course of development. In such a case, the correct measure of damages is the difference in value, and not the cost of performance. However, this leads to the exact problem which Cotter presented. What the Court really did was limit the aggrieved party’s expectation interest to what he could prove — and how can one prove speculative damages and lost reliance on a chance of finding oil? This, of course, takes us back to the “lost chance” or “speculative damages” problem. Had the Court taken notice of the Kinkel and Chaplin cases, then Cotter’s failure to prove that he had been deprived of some reasonable probability of realizing an advantage of some real substantial monetary value would have meant, on the facts of the case, that he could only recover nominal damages.

The Court seemed to have pre-decided that Cotter would not, in any event, get the cost of performance; the reasons are obvious: Cotter did not, to a significant degree, seek substitute performance; he did not attempt to mitigate; and the award of the cost of performance might have been a windfall recovery as it was doubtful (or impossible) that he would have had the work done in any event. All these factors should be considered; but why did the Court hide them? The same result could have been achieved by applying the Cunningham test and by ignoring the adequacy or passing of consideration. The Supreme Court’s decision has done nothing other than confuse the issue by bringing in new terms and tests. Since this type of case does not come before the Supreme Court of Canada very often, the only recourse which the Court possesses is simply to distinguish the Cotter case and to apply the Cunningham case on the basis of factual distinction, and this is exactly what the Court has done some twenty years later in its most recent decision. However, we shall get to that soon enough.

Before leaving Cotter and all its complexities, there is one further point related to the problem of nominal versus substantial damages. In the case of Prudential Trust Co. Ltd. and Wagner v. Wagner Oils Ltd., McLaurin, C.J.T.D., who was the trial Judge in the Cotter case, dealt with the breach of a contract in which the defendant had an absolute commitment to drill an oil well in the following manner:

If it were not for the Cotter decision, I would be disposed to fix the damages at some substantial amount, probably the cost of drilling a well. I still see nothing unfair in visiting a defaulting party with damages in this amount. The whole foundation of legitimate promotional efforts in the exploitation of oil are based

48 On the facts of Cotter, the Cunningham test as proposed might have been a bit difficult to apply. The evidence in the case was that the plaintiff had been in negotiation with an oil company; however, there was no evidence as to the terms offered by the company. Cartwright and Fauteux, J.J., were influenced by the fact that the plaintiff had not delayed bringing his action until the arrangements to have the well drilled by the oil company had been completed. The plaintiff tendered no concrete evidence on his negotiations with the oil company and made no request in the Alberta Supreme Court, Appellate Division, for a reference to fix the damages. Thus, it seems that these two judges in fact considered that the plaintiff had abandoned any attempt to have the work completed in the ordinary course of development; therefore, this branch of the Cunningham test can be reconciled with the facts in Cotter.

49 See, discussion supra.

50 See, discussion infra.

on the assumption that the parties will not renege on such deals. However, the Cotter case has established that such damages must not be awarded, but it does hold that nominal damages are recoverable even though no nominal damages were fixed in that case.\footnote{Id. at 374.}

However, in the later case of Albrecht v. Imperial Oil Ltd.,\footnote{(1957), 21 W.W.R. 560 (Alta.S.C.).} the trial Judge held that the Cotter case did not prohibit him from fixing substantial damages.\footnote{Id. at 566 per Riley, J.}

These two decisions only serve to show how the Cotter decision has caused confusion by its misinterpretation. The Cotter case did not establish that substantial damages would never be awarded; it simply established that only nominal damages will be awarded if the absence of proof makes damages a matter of speculation.\footnote{See also Krang v. McCutcheon (1920), 19 O.W.N. 161 (Ont.C.A.).} The trial judge's interpretation of Cotter in the Prudential Trust case was an unjustifiable extension of the Cotter principle.\footnote{J. Ballem, Petroleum and Natural Gas Lease — Damage for Breach of Drilling Commitment (1957), 35 Can. Bar Rev. 971, 976.}

There has been a vast number of articles written in the United States dealing with the measure of damages for breach of a covenant to drill a test well.\footnote{For United States articles on the measure of damages for breach of a contract to drill an oil or gas well, see: 4 A.L.R. (3d) 284; 9 U. of Kansas L.Rev. 281 (1960-61); 1959 U. of Ill. Law Forum 631; 13 Wash. & Lee L.Rev. 207 (1956); 3 U.C.L.A. L.Rev. 586 (1955-56); 8 Wyom. L.J. 142 (1953-54); 22 Tex.L.Rev. 481 (1944).} There the damages aspect of such cases is dealt with in three categories depending upon the intent of the parties: (1) where the defendant has been employed to drill a well on a contract basis and has no interest in the possible future production; (2) where a lease assignment has been made based on the expectation of future royalties, the consideration for the lease being the lessee's agreement to drill a well; and (3) where the plaintiff is interested in a test well on his property and in the effect of such a well on adjoining property owned or leased by the plaintiff (the "information contract" situation).

In the first situation the courts generally hold the measure of damages to be the difference between the reasonable cost of drilling or completing the well less any part of the contract price remaining unpaid. This resembles the measure of damages given a landowner in a suit against a builder under an ordinary construction contract.

In the second and third situations the courts have adopted divergent rules. Certain states award the cost of drilling; however, this measure is in conflict with the ordinary rule of damages. Where a well drilled under the contract would have produced oil which the plaintiff can no longer extract, he is left without adequate compensation. Conversely, if the cost of drilling would be more than the royalties which would have resulted, the plaintiff gets over-compensation. However, if the award given is based on expected royalties and the plaintiff continues drilling which results in production leading to these royalties, then the plaintiff gets double recovery. Then
comes the evidentiary problem of establishing the quantum of the lost royalties.

These problems have led many authors to support the "cost of drilling" as the proper measure of damages. For example, one author gives this rationale:

It was a recognition of the practical impossibility of an obligee's proving the future productivity of a test well that led a majority of states to adopt the "well-cost" rule. Most courts admit that the cost of drilling is not always an accurate measure of the obligee's injury, but state that it is capable of reasonably exact computation, and that to force the obligee to prove his actual damages would in effect deny him any remedy for the breach of contract or would allow the jury to indulge in guesswork as to the amount of damages.\(^5\)

Another author has this to say:

... there should also be a more general recognition of the necessity of striking a proper balance between the value of the unrendered performance of the uncertainty of proof of damages caused by defendant's breach. In many cases it is submitted that this can be accomplished by treating the reasonable cost of drilling or completing the well as a \textit{prima facie} measure which might have the effect of discouraging drilling defaults.\(^6\)

It is respectfully submitted that the Canadian courts should also adopt such an approach.

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PART IV

\textit{The New Horizons — Realistic and Defined Approaches to the Problem}

In 1962, an unusual fact situation arose before the British Columbia Supreme Court in the case of \textit{Worrall v. Northwestern Mutual Insurance Co.}\(^7\)

In this case the plaintiff had his property insured by the defendant company against fire loss. The policy provided that on the occurrence of a loss by fire the insurer could elect to repair and rebuild the property instead of making payment.

In considering the obligations which an insurer against fire loss undertakes when it elects, as the defendant did, to repair instead of making payment, and the measure of damages if it fails in fulfilling those obligations, Hutcheson, J. reviewed a number of American decisions in the absence of Canadian and English authority. The learned judge avoided the problems of consideration, benefits, essential terms of an overall plan, substantial performance, and economic waste which the Courts have grappled with in the cases I have already discussed. He first defined the obligation of the defendant in simple, yet precise terms:

... the defendant, having elected to repair, was under the duty to repair the property so that it would be in substantially as good a condition as it was prior to the fire.\(^8\)


\textsuperscript{6}W. Scott, \textit{Measure of Damages for Breach of a Covenant to Drill a Test Well for Oil and Gas} (1960-61), 9 U. of Kansas L.Rev. 281, 291.

\textsuperscript{7}(1963), 36 D.L.R. (2d) 752; (1963), 41 W.W.R. 284 (B.C.S.C.).

\textsuperscript{8}Id. at 756, 41 W.W.R. at 287.
The obligation is clear enough: the defendant must give the plaintiff essentially what he bargained for — a house built in a certain specified manner.

Then, in considering the measure of damages, he defined the two situations which may arise:

1. If the insurer fails to rebuild or repair after electing to do so, or abandons the work before it is finished, the measure of damages for breach of its obligation is the cost of doing or completing the work.

2. If the repairs are completed but the house as delivered to the insured is not in substantially the same condition as it was in before the fire, his measure of damages is the difference in value of the house as it stood before the fire and its value at the time the insurer offered it to the insured and ceased to perform labour on it.0

The two situations are quite clear. If the insurer has given substantial performance and the insured gets something approximating what he bargained for, then his only compensation is in damages for the difference in value. However, if no performance has been given, the insured must be placed in a position similar to that which he occupied when the contract was made — i.e., he must have a house similar to the original one. Therefore, the cost of building such a house is the correct measure. The insured must have the house because this was the essential root of the contract. Therefore, the doctrine of substantial performance definitely affects the measure of damages.

A recent example of how the doctrine of substantial performance affects the measure of damages is found in Miller v. Advanced Farming Systems Ltd.0 The facts of that case were straightforward. The plaintiff dairy farmer contracted with the defendant company to have a dairy barn complex constructed according to specified plans and measurements. The trial judge found, as a fact, that the work had not been done as called for in the contract, but that there had been substantial performance. He thereupon applied the doctrine of substantial performance by allowing the defendant his contract price, less credit to the plaintiff for the deficiencies in the work. Thus, he applied the difference in value as the correct measure of damages.

However, in the Supreme Court of Canada, Hall, J. cited authorities6 which stated that the correct measure of damages “is the cost of making good the defects and omissions in the work which the respondent contracted to do.”0 Therefore if the contractor is able to show that there has been substantial performance, then he is entitled to recover his contract price subject to a deduction equivalent to the cost of altering the work to make it correspond with the contract specifications.

Thus, the cost of performance is often given as the measure of damages in building contracts. However, the courts have rarely outlined any clear criteria upon which this measure will be awarded. An exception was McGarry

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0 Id. at 756-760, 41 W.W.R. at 287-294.
where the British Columbia Supreme Court finally defined the conditions under which the cost of performance will be allowed. Again, as in the Worrall case, the test laid down was simple and without reference to the confusing jargon which had been so predominant in previous years.

In the McGarry case there was poor workmanship and a deviation from the plans by the builder in the construction of an apartment building. In response to the submission by counsel for the plaintiff that the measure of damages should be the cost of making good the defective work, Davey, J. laid down several simple rules to determine whether or not damages will be awarded on this scale. First, the cost of performance should not be awarded where the owner does not intend to, or cannot rectify or complete the defective work, or where he would be acting unreasonably or oppressively in doing so. The policy behind this principle is obvious — the court will not encourage economic waste or unjust enrichment. Second, in speaking of the Cunningham and Cotter decisions, Davey, J. said,

These cases establish that the primary measure of damages for non-performance of a contract to build on another's land is the diminution in value resulting from such default. In the case at bar, the work was imperfectly done, but, I can see no difference in principle.

Cases may arise where the damages for the default should be measured by the cost of making good the default. This will be so if the cost of performing the work or making good the defects is less than the diminution in the value of property caused by the default. In such cases, it is the plaintiff's duty to take any reasonable steps to mitigate his damage by doing what is required.

Other cases arise where a person's enjoyment of his property is substantially lessened by the non-performance or the defective performance of the work, and it is reasonable that he should have the work done even though its cost may exceed the decrease in the market value of the property resulting from the default. In such cases, the plaintiff is entitled to the cost of doing the work, if it appears that he intends to, or is likely to have it done, providing he acts reasonably.

The key word in this approach is the word "substantially". We have discussed the implication of this word previously. The meaning should be obvious — the Court will award the cost of performance if what the innocent party received is not substantially what he bargained for. And in deciding whether or not the plaintiff got substantially or essentially what he bargained for, Davey, J. applies this test:

I think the likelihood of the plaintiff doing the work must always be considered before adopting the cost of remedying the default as the measure of damages, except where that measure is applied by way of mitigation of damages. Also, the reasonableness of doing the work must be judged not only by the effect of the default upon the amenities of the property, but by the relation between the cost of repairing the default and the diminution in the value of the premises caused by it.

Thus, the learned judge lays down two simple principles. First, the higher award of the cost of performance will not be made if it is unlikely that the plaintiff will have the work performed. Secondly, the high costs will not be awarded solely on the basis of a party's not getting what he bargained for —

70 Id. at 391.
if the cost of performance is out of all proportion to the damage caused, then the diminution in value will be awarded. Again, the policy is obvious — the Court will not encourage economic waste.

Thus, it took over half a century, since the 1882 Wiggsell case, for a Canadian court to finally define the law to be applied for the measure of damages in building contracts\(^1\) in terms which avoid the usual judicial jargon, and which face the problem realistically from both an economic and commonsense point of view.

The position in the United States\(^2\) has been dealt with extensively. In actions for an owner's recovery for breach of a building contract, the following principles apply.\(^3\) Generally, where the contractor abandons a building contract, the measure of damages available to the owner is the reasonable cost of completion less any part of the contract price remaining unpaid. However, if the construction is defective, the owner can recover the reasonable cost of construction in accordance with the contract less such part of the contract price as has not been paid.\(^4\) But if to complete the defective construction would involve unreasonable economic waste, the owner can recover only the amount by which the value of the house as left by the builder fell short of what the value would have been if the contract had been exactly performed, less any part of the contract price remaining unpaid. These principles certainly support the position taken by the Ontario courts in the O'Brien case\(^5\) with regard to the economic waste and benefit arguments. However, in the case of wilful breaches it has been suggested that the cost of performance may be granted even if uneconomic.\(^6\)

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One of the more notable cases decided in the United States with regard to contracts to do work or land construction is: Groves v. John Wunder Co. (1935), 205 Minn. 163, 286 N.W. 233; for critical case comments see: (1940), 40 Colum.L.Rev. 323; (1939-40), 25 Cornell L.Q. 287; (1939-40), 53 Harv.L.Rev. 138; (1939-40), 34 Ill.L.Rev. 501; but for a favourable case comment see (1939-40), 24 Minn.L.Rev. 114. For a similar set of facts but an opposite decision to the Groves case, see Avery v. Fredericksen and Westbrooke (1944), 154 P. (2d) 41 (Cal.App.) and the case comment at (1944-45), 43 Mich.L.Rev. 987. See also Peevyhouse v. Garland Coal and Mining Co., Okl. 382 P.(2d)109; aff'd on rehearing, Okl., 382 P.(2d)116 and the case comment comparing the case to the Groves case: Damages — Measure of Damages — Cost of Performance versus Diminution in Value for Breach of a Strip-Mining Lease (1964), 49 Iowa L.Rev. 597.


\(^4\) This is also the position taken in England: Contracts for the Execution of Work: Effect of Non-Completion (1955), 22 The Solicitor 153.

\(^5\) (1923), 54 D.L.R. 455 (Ont.C.A.).

The conflict in the measure of damages also arises when realty or personality is physically damaged or totally destroyed. The generally accepted rule in cases of realty is that the normal measure of damages is the diminution in the value of the property. Generally, this rule has been applied to the case of an occupier of the real property. However, there have been several exceptions where owner-occupiers of realty have been able to recover the cost of restoring buildings damaged by a defendant's trespass. The English Court of Appeal recently considered this problem in Harbutt's "Plasticine" Ltd. v. Wayne Tank and Pump Co. Ltd. In that case the defendant company contracted to install equipment in the plaintiff company's factory; however, due to the defendant company's negligence, the whole factory was destroyed by fire and a new factory had to be built. The defendants claimed that the plaintiffs were entitled only to the difference in value of the old factory before and after the fire (£116,785) rather than the actual cost of replacement (£146,581). However, the Court had no trouble in deciding that the plaintiffs were entitled to the cost of replacement:

"If the article damaged is a motor car of popular make, the plaintiff cannot charge the defendant with the cost of repair when it is cheaper to buy a similar car on the market. On the other hand, if no substitute for the damaged article is available and no reasonable alternative can be provided, the plaintiff should be entitled to the cost of repair."

The policy here is again apparent. First, the purpose of damage awards in such cases is to restore the plaintiff to the position he occupied before the loss occurred (i.e. restitution). Thus, if he has lost a chattel, then a replacement can usually be found in the market and the owner gets the value; but if he has lost a building, then a replacement must be constructed and the owner gets the cost of replacement. To award the owner the cost of replacement when a substitute chattel is available would be tantamount to encouraging unjust enrichment.

The "failure to drill" problem and the confusion raised by the Cotter decision have finally been met head-on in Dolly Varden Mines Ltd. (N.P.L.) v. Sunshine Exploration Ltd. et al., a recent decision of the Supreme Court of Canada. After nearly twenty years of confusion, the Court utilized the one recourse which it possessed and to which I referred earlier — it distinguished the Cotter case and applied the Cunningham doctrine. In the case the plaintiff was the owner of certain mining properties and agreed with the defendants to convey a one-half interest in the properties in return for certain exploratory drilling work to be carried out by the defendants. The defend-

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82 See, discussion supra at 193.
ants were to furnish reports of all the work done and were also given the option, after completion of the first phase of the work (schedule "A"), either to abandon the project or to continue with the subsequent phases. Having undertaken a small portion of the work and finding the preliminary results disappointing, the defendants breached the agreement by not performing the first phase of the work (schedule "A"). In the original action for damages, the trial Judge applied the Cunningham principle to award $314,051 based upon the cost to the plaintiffs of having the work performed. The award was upheld in the Court of Appeal of British Columbia and thus the sole issue before the Supreme Court of Canada was the correct measure of damages to be applied.

Martland, J., in delivering the judgment of the Court, quickly distinguished Cotter on the basis that consideration had passed in full in the instant case but that in Cotter no consideration had ever passed. In the present case the defendant had received full consideration (the transfer of the one-half interest in the properties), but had failed to perform the schedule "A" work as promised. And with that distinction, the death-knell of Cotter was finally sounded.

Martland, J. then considered exactly what the plaintiffs lost by reason of the defendant company's default. He pointed out that Sunshine had committed itself to perform the work because it considered the results would be of value. Dolly Varden gave full consideration because it would be able to further develop its property if the results were favourable; if the results were unfavourable, then the company would still have obtained valuable information about the property. However, both parties clearly considered that the work to be performed would be worth the expense of doing it. Thus, Martland, J. explored the intentions of the parties — to perform work of a definite specified nature. The first requirement of the Cunningham rule was met — the work to be performed was part of an overall scheme of works, the execution of which was necessary for the proper development of the property. The second part of the rule — that it could fairly be presumed that the owner intended to carry out the work — was shown both by the intention and the post-breach conduct of Dolly Varden. However, although the case could easily be squared with Cunningham, Martland, J. preferred not to lay down any general rule with regard to damages sustained by a mine owner for breach of a covenant to perform exploratory or development work. Nevertheless, there is little doubt that the essence of the decision is to adopt the Cunningham rationale and to award the cost of performance as the proper measure of damages in such a case. Furthermore, it should be recalled that the Cunningham rationale was based on no special rule but an application of the general rule of awarding the expectation interest.

Keeping this in mind, it is not difficult to understand how the Court reached its decision to award damages based on the cost of performance:

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83 (1969), 8 D.L.R. (3d) 441 at 450.
85 See supra notes 37-38, and see discussion supra at 189-190.
When Sunshine, later, deliberately breached its contract to perform the work, what was the measure of Dolly Varden's damage? If it had paid cash for the work, it would clearly be entitled to a repayment of it, and would also have a claim in damages. The consideration was not in cash, but Sunshine, when it executed the amending agreement, considered it to be of sufficient value to warrant the expenditure necessary to perform the work.

It is pointless, in these circumstances, to suggest that a comparison be made between the value of the mining property with and without the work being done. The result of the sch. A work is unknown, and it is unknown because Sunshine elected to break the contract for its performance. But when Sunshine, by entering the agreement, acknowledged that, in the light of its future potential benefits under the agreement, its own suggested programme of work was worth the cost of performing it, and when Dolly Varden was prepared to give, and did give, valuable consideration for its performance, I consider that it was entirely proper for the learned trial Judge to assess the damage resulting from the breach as being equivalent to the cost of doing the work. In so doing he was seeking to fulfill the underlying principle stated by Lord Atkinson in Wertheim v. Chicoutimi Pulp Co., [1911] A.C. 301 at p. 307, and cited by Cartwright, J., in the Cotter case . . .

Thus, we go back to the very beginning. The Wertheim rule seeks to place the parties in the same position as if the contract had been performed. If the contract had been performed then Dolly Varden would have received the value of the information concerning the worth of its properties. The only way by which Dolly Varden could have received this information was to have the development work done. And the only way to compensate for not having the work done is to award the cost of performing the work. It follows then that the appropriate measure of damages is the cost of performance rather than the difference in value.

Therefore, the result of Dolly Varden is this — Cotter is buried, Cunningham is revived, and Wertheim reigns supreme. But the difficulty of applying Wertheim when the cost of performance is in conflict with the difference in value will probably live forever.
