Title:
Dunlop Pneumatic Tyre Co., Ltd. v. New Garage and Motor, Ltd., [1915] A.C. 79

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The House took time for consideration.

July 1. **LORD DUNEDIN.** My Lords, the appellants, through an agent, entered into a contract with the respondents under which they supplied them with their goods, which consisted mainly of motor-tyre covers and tubes. By this contract, in respect of certain concessions as to discounts, the respondents bound themselves not to do several things, which may be shortly set forth as follows: not to tamper with the manufacturers' marks; not to sell to any private customer or co-operative society at prices less than the current price list issued by the Dunlop Company; not to supply to persons whose supplies the Dunlop Company had decided to suspend; not to exhibit or to export without the Dunlop Company's assent. Finally, the agreement concluded (clause 5), "We agree to pay to the Dunlop Pneumatic Tyre Company, Ltd. the sum of 5 *l*. for each and every tyre, cover or tube sold or offered in breach of this agreement; as and by way of liquidated-damages, and not as a penalty." The appellants, having discovered that the respondents had sold covers and tubes at under the current list price, raised action and demanded damages. The case was tried and the breach in fact held proved. An inquiry was directed before the Master as to damages. The Master inquired, and assessed the damages at

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250 *l*., adding this explanation: "I find that it was left open to me to decide whether the 5 *l*. fixed in the agreement was penalty or liquidated damages. I find that it was liquidated damages."

The respondents appealed to the Court of Appeal, when the majority of that Court, Vaughan Williams and Swinfen Eady L.JJ., held, Kennedy L.J.(dissenting, that the said sum of 5 *l*. was a penalty, and entered judgment for the plaintiffs for the sum , of 2 *l*. as nominal damages. Appeal from that decision is now before your Lordships' House.

My Lords, we had the benefit of a full and satisfactory argument, and a citation of the very numerous cases which have been decided on this branch of the law. The matter has been handled, and at no distant date, in the Courts of highest resort. I particularly refer to the *Clydebank Case*[1] in your Lordships' House and the cases of *Public Works Commissioner v. Hills*[2] and *Webster v. Bosanquet*[3] in the Privy Council. In both of these cases many of the previous cases were considered. In view of that fact, and of the number of the authorities available, I do not think it advisable to attempt any detailed review of the various cases, but I shall content myself with stating succinctly the various propositions which I think are deducible from the decisions which rank as authoritative:-

1. Though the parties to a contract who use the words "penalty" or "liquidated damages" may prima facie be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages. This doctrine may be said to be found passim in nearly every case.

2. The essence of a penalty is a payment of money stipulated as in terrorem of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage (*Clydebank Engineering and Shipbuilding Co. v. Don Jose Ramos Yzquierdo y Castaneda*[1]).

3. The question whether a sum stipulated is penalty or liquidated damages is a question of construction to be decided

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upon the terms and inherent circumstances of. each particular contract, judged of as at the time of the making of the contract, not as at the time of the breach *(Public Works Commissioner v. Hills*[1] and *Webster v. Bosanquet*[2]).

4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are

(a) It will be held to be penalty if, the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach. (Illustration given by Lord Halsbury in *Clydebank Case*.[3])

(b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid (*Kemble v. Farren*[4]). This though one of the most ancient instances is truly a corollary to the last test. Whether it had its historical origin in the doctrine of the common law that when A. promised to pay B. a sum of money on a certain day and did not do so, B. could only recover the sum with, in certain cases, interest, but could never recover further damages for non-timeous payment, or whether it was a survival of the time when equity reformed unconscionable bargains merely because they were unconscionable, -a subject which much exercised Jessel M.R. in *Wallis v. Smith*[5]- is probably more interesting than material.

(c) There is a presumption (but no more) that it is penalty when " a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage " (Lord Watson in *Lord Elphinstone v. Monkland Iron and Coal Co.*[6]).

On the other hand

(d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such

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as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties (*Clydebank Case*, Lord Halsbury[1]; *Webster v. Bosanquet*, Lord Mersey[2]).

Turning now to the facts of the case, it is evident that the damage apprehended by the appellants owing to the breaking of the agreement was an, indirect and not a direct damage. So long as they got their price from the respondents for each article sold, it could not matter to them directly what the respondents did with it. Indirectly it did. Accordingly, the agreement is headed "Price Maintenance Agreement," and the way in which the appellants would be damaged if prices were cut is clearly explained in evidence by Mr. Baisley, and no successful attempt is made to controvert that evidence. But though damage as a whole from such a practice would be certain, yet damage from any one sale would be impossible to forecast. It is just, therefore, one of those cases where it seems quite reasonable for parties to contract that they should estimate that damage at a certain figure, and provided that figure is not extravagant there would seem no reason to suspect that it is not truly a bargain to assess damages, but rather a penalty to be held in terrorem.

[...]

[1][1905] A. C. 6
[2][1906] A. C. 368.
[3][1912] A. C. 394.
[1][1906] A. C. 368.
[2][1912] A. C. 394.
[3][1905] A. C. 6.

[4]6 Bing. 141.
[5]21 Ch. D. 243.
[6]11 App. Cas. 332
[1][1905] A. C. at p. 11.
[2][1912] A. C, at p. 398.

Referring Principles:

VI.4 - Promise to pay in case of non-performance

IX.1 - Basic rule