

DAMAGES: "VALUE OF THE CONTRACT," A NOVEL  
STANDARD FOR ASSESSING DAMAGES RESULTING FROM  
FRAUDULENTLY INDUCED PERSONAL SERVICE  
CONTRACTS

IN the recent case of *Espaillet v. Berlitz Schools of Languages of America, Incorporated*,<sup>1</sup> the Court of Appeals for the District of Columbia Circuit synthesized tort and contract theories to produce a novel standard for the assessment of damages. Defendant Berlitz fraudulently induced Espaillet to enter into a one-year service contract to teach at a United States Army language school by assuring her that her Dominican Republic citizenship would have no effect on her future employment. Two months later, upon discovery of her alien status, the Army, in accordance with its established policy of which Berlitz had knowledge, forced Berlitz to terminate her employment. Following the expiration of the contract period, Espaillet filed a complaint in the District of Columbia Court of General Sessions alleging breach of contract. Later she restated her claim on the ground of fraud, apparently in reliance upon the successful employment of a fraud theory in a parallel case, *Andolsun v. Berlitz Schools of Languages of America, Incorporated*,<sup>2</sup> involving another language instructor dismissed under similar circumstances. Subsequent to a damage award of \$2,000 by a jury, the court granted a motion for a judgment n.o.v. in favor of Berlitz.<sup>3</sup> Since Espaillet had failed to prove previous earnings, an element of damages essential to recovery under a fraud theory in the District of Columbia, the District of Columbia Court of Appeals affirmed the judgment;<sup>4</sup> but the Court of Appeals for the District of Columbia Circuit, rejecting traditional damages standards as inapplicable, reversed and ordered a new trial limited to assessment of damages under the criteria which it established.<sup>5</sup>

Damages for an employer's breach of a personal service contract are ordinarily based upon the amount of wages that would have been

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<sup>1</sup> 383 F.2d 220 (D.C. Cir. 1967).

<sup>2</sup> 196 A.2d 926 (D.C. App. 1964).

<sup>3</sup> *Espaillet v. Berlitz Schools of Languages of America, Inc.*, 217 A.2d 655, 656 (D.C. App. 1966).

<sup>4</sup> *Id.* at 658.

<sup>5</sup> 383 F.2d at 224.

paid but for the breach.<sup>6</sup> Added to this amount are consequential damages, such as the employee's cost of procuring new employment,<sup>7</sup> less wages earned during the remainder of the contract period following the breach.<sup>8</sup> Had the plaintiff in *Espaillet* not modified her suit on the contract, her recovery would have been approximately \$3,500: \$6,000 in unpaid wages, plus a \$250 cost of procuring new employment, less \$2,750 earned after the breach.<sup>9</sup> In a tort action for fraudulent misrepresentation, on the other hand, a plaintiff is entitled to recover damages for all losses naturally and proximately resulting from the fraud.<sup>10</sup> Two standards have been used to measure the proximity of the loss to the fraud. The "out of pocket" or tort standard, applied by the English courts in the common law action of deceit,<sup>11</sup> and by a minority of American jurisdictions,<sup>12</sup> contemplates placing the victim in a position equivalent to that existing before the inception of the fraudulent contract.<sup>13</sup> Under this standard a party injured by breach of a fraudulently induced personal service contract could recover the earnings sacrificed in order to enter the contract,<sup>14</sup> less the aggregate of wages earned pursuant to the contract and following the breach, plus the cost of securing new employment.<sup>15</sup> A more liberal damage standard, traditionally applied in tort to fraudulent real and personal property sales transactions,<sup>16</sup> is the "benefit of the bargain" rule, which focuses upon the representations made and attempts to award the fraud

<sup>6</sup> See 4 A. CORBIN, CONTRACTS § 958 (1951); 2 T. SEDGWICK, DAMAGES § 667 (9th ed. 1913); 3 S. WILLISTON, CONTRACTS §§ 1358-59 (rev. ed. 1937).

<sup>7</sup> E.g., *Beggs v. Dougerty Overseas, Inc.*, 287 F.2d 80, 83 (2d Cir. 1961); see 5 A. CORBIN, CONTRACTS § 1044 (1964); C. McCORMICK, DAMAGES § 163 (1935).

<sup>8</sup> See 5 A. CORBIN, CONTRACTS § 1039 (1964); C. McCORMICK, *supra* note 7, § 158.

<sup>9</sup> For the true values see 383 F.2d at 221 n.2, 222, 224 n.11.

<sup>10</sup> See *Sigafus v. Porter*, 179 U.S. 116, 122-23 (1900); *Smith v. Bolles*, 132 U.S. 125, 129 (1889); W. PROSSER, TORTS § 105 (3d ed. 1964); Note, *Measure of Damages for Fraud and Deceit*, 47 VA. L. REV. 1209 (1961); Note, 22 B.U.L. REV. 295, 298 (1942).

<sup>11</sup> See *McConnel v. Wright*, [1903] 1 Ch. 546; *Peek v. Derry*, 37 Ch. D. 541 (1887), *rev'd on other grounds*, 14 App. Cas. 337 (1889).

<sup>12</sup> See *McCormick, Damages in Actions for Fraud and Deceit*, 28 NW. U.L. REV. 1050, 1052 & nn.11-16 (1934); Note, *Measure of Damages for Fraud and Deceit*, 47 VA. L. REV. 1209, 1212 & n.16 (1961).

<sup>13</sup> See C. McCORMICK, *supra* note 7, § 121; W. PROSSER, *supra* note 10, at 751; *McCormick, supra* note 12, at 1051; *Rossen & Fairweather, Damages in Fraud Actions*, 13 CLEV.-MAR. L. REV. 288 (1964).

<sup>14</sup> See authorities cited note 13 *supra*.

<sup>15</sup> See notes 7-8 *supra* and accompanying text.

<sup>16</sup> E.g., *Ren v. Jones*, 38 Ariz. 476, 479, 1 P.2d 110, 111 (1931); *Kendrick v. Ryus*, 225 Mo. 150, 160, 123 S.W. 937, 941 (1909); *Gunther v. Ullrich*, 82 Wis. 222, 223, 52 N.W. 88, 89 (1892).

victim the value of his frustrated expectations.<sup>17</sup> Under this theory, adopted by a majority of the states,<sup>18</sup> the defrauding defendant is viewed as warranting the truth of his statements. Thus plaintiff's recovery is based on the difference between the represented value and the consideration actually delivered by the defrauder. To this would be added the cost of procuring new employment, less wages received subsequent to the breach of contract.<sup>19</sup>

The amending of the complaint in *Espaillet* from breach of contract to fraudulent inducement would have had no effect upon the amount of *Espaillet's* recovery if the requested "benefit of the bargain" standard had been applied, for the elements of damage computation are identical under either approach. Hypothetically, *Espaillet* would have been awarded \$3,500 damages under either theory.<sup>20</sup> Unfortunately for *Espaillet*, however, the District of Columbia courts have rejected the "benefit of the bargain" theory and adopted the "out of pocket" standard.<sup>21</sup> Since the awarding of "out of pocket" damages is based upon the earnings sacrificed in order to enter the contract, recovery is dependent upon the successful establishment of a pre-contract employment record.<sup>22</sup> To obtain a recovery equal to that obtainable under the contract theory, a plaintiff's pre-contract wage level must equal the contract wage.<sup>23</sup> Due to the part-time nature of *Espaillet's* previous employment, she was unable to establish adequately the value of her previous earnings, and under existing law was consequently barred from recovering damages.

The Court of Appeals for the District of Columbia Circuit, in reversing, established that in light of the fraudulent misrepresentations by Berlitz, and the successful recovery in the *Andolsun* case,<sup>24</sup> the lack of a clear comparison between wages earned before and after

<sup>17</sup> See McCormick, *supra* note 12, at 1053 & n.18; Rossen & Fairweather, *supra* note 13, at 291; Note, *Measure of Damages for Fraud and Deceit*, 47 VA. L. REV. 1209, 1220-21 (1961); Note, 22 B.U.L. REV. 295, 298 (1942).

<sup>18</sup> See McCormick, *supra* note 12, at 1052-53 & n.18; Note, *Measure of Damages for Fraud and Deceit*, 47 VA. L. REV. 1209, 1210 & n.7 (1961); Note, 26 CORNELL L.Q. 133, 134 & n.9 (1940).

<sup>19</sup> See notes 7-8 *supra* and accompanying text.

<sup>20</sup> See notes 6-9 *supra* and accompanying text.

<sup>21</sup> *Espaillet v. Berlitz Schools of Languages of America, Inc.*, 217 A.2d 655, 657 (D.C. App. 1966).

<sup>22</sup> *Id.*

<sup>23</sup> See notes 6-8, 14-15 *supra* and accompanying text.

<sup>24</sup> See note 2 *supra* and accompanying text.

the contract was not a compelling ground for the total denial of a remedy.<sup>25</sup> Finding merit in Supreme Court dissatisfaction with the traditional damage standards as applied in securities fraud cases,<sup>26</sup> the circuit court determined that neither the "out of pocket" nor the "benefit of the bargain" standard provided "an apt gauge for recovery" in the case of a fraudulently induced service contract.<sup>27</sup> A proper measure of damages, the court indicated, would be based upon the "value of the contract" to *Espaillet*; and this value, unlike value under the "benefit of the bargain" standard, is not fixed by the proposed contract salary.<sup>28</sup> The court concluded that three factors are to be weighed by the jury in its determination of this value—the plaintiff's qualifications; the worth of the plaintiff's services as evidenced by her previous experience, proposed contract wages, and the value given to her services following the breach of contract; and the "earning power" of the plaintiff in the various services she would have performed under the contract.<sup>29</sup> In addition, the plaintiff's recovery would include the cost of procuring new employment after the breach. The aggregate of these consequential damages and the value of the contract would be reduced by wages earned pursuant to the contract and following the breach to determine the amount of the award.

Since juries are often called upon to assess the value of services in *quantum meruit* and to determine the value of such abstract items as mental anguish or physical pain,<sup>30</sup> the standard fashioned by the *Espaillet* court seems neither too speculative nor too difficult to apply. In addition, the risk of inexactitude has traditionally fallen on the defrauding defendant rather than on an innocent victim of the fraud.<sup>31</sup> The opinion does not, however, resolve the issue of the precise breadth of discretion given the jury in valuing the contract. In addition to elements mentioned in the opinion, other factors, such as job security, working conditions, business contacts, and

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<sup>25</sup> 383 F.2d at 222-23.

<sup>26</sup> *Id.* at 222, citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963).

<sup>27</sup> 383 F.2d at 223.

<sup>28</sup> *Id.*

<sup>29</sup> *Id.* at 224.

<sup>30</sup> *E.g.*, *Fowler Rental Equip. Co. v. Skipper*, 276 Ala. 593, 604, 165 So. 2d 375, 386 (1964); *Franco v. Fujimoto*, 47 Hawaii 408, 424, 390 P.2d 740, 750 (1964).

<sup>31</sup> *See Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 265 (1946); *Story Parchment Co. v. Paterson Parchment Paper Co.*, 282 U.S. 555, 563 (1931).

personal satisfaction, may be relevant in determining the "value of the contract" to the plaintiff, and seemingly should be considered. In any event, it seems unlikely that a jury would determine the value of an employment contract to a defrauded plaintiff to be less than the wages promised. The minimum recovery, therefore, can be expected to equal the amount awarded in an action based on breach of contract, or on fraudulent inducement to contract, when damages are measured by the "benefit of the bargain" standard. On the other hand, the "value of the contract" *could* be found to be significantly greater than the contract wages proposed. Thus, the attorney who is willing to accept the additional burden of proof required to establish fraud may find it advantageous in a suit on a fraudulently induced personal service contract to plead fraudulent inducement as an alternative ground for recovery, and seek application of the "value of the contract" standard applied in *Espaillet*.