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NJ Now Allows New Businesses To Recover Lost Profits Established With a 'Reasonable Degree of Certainty'

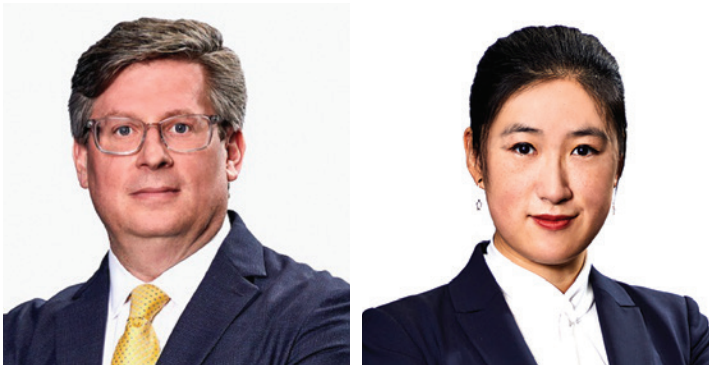
By a decision issued on Aug. 17, 2022, in 'Schwartz v. Menas,' the Supreme Court of New Jersey joined the majority of other jurisdictions in finding that a per se ban on lost profits damages by a new business is unwarranted.

By Elliot D. Ostrove and Lucia Wa Yang

New Jersey long followed the "new business rule," adopted by the Court of Errors & Appeals in *Weiss v. Revenue Building & Loan Association*, 116 N.J.L 208 (E. & A. 1936), which effectively barred claims for lost profits by new businesses because the court found, such claim cannot be proven with reasonable certainty. In *Weiss*, the Court of Errors & Appeals noted that in new businesses, "the prospective profits are too remote, contingent and speculative to meet the legal standard of reasonable certainty." *Id.* at 210, 212.

In the decades since *Weiss*, courts in other jurisdictions have concluded that, although it is difficult for a new business to meet the standard of reasonable certainty, a *per se* ban on lost profits damages by a new business is unwarranted. Rather, those courts carefully scrutinize such claims, treating a new business' inexperience as an important factor in the "reasonable certainty" standard.

By a decision issued by the Supreme Court of New Jersey on Aug. 17, 2022, *Schwartz v. Menas*, 2022 N.J. LEXIS 675 (Aug. 17, 2022), New Jersey joined the majority of other jurisdictions and found that, "[t]o the extent that *Weiss* can be read to adopt a *per se* bar on all lost profit damages claims by new businesses, we depart from the test prescribed by the Court of Errors and Appeals."



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In *Schwartz*, plaintiff Larry Schwartz is an owner of a dry cleaning business who had never acted "as a developer." Schwartz commenced two separate actions, alleging that the defendants in each action deprived him of the opportunity to construct and develop certain real properties, causing him to suffer lost profit damages.

In both actions, Schwartz retained the same expert, Dr. Robert Powell, and served a lost profits damages expert's report. In both reports, Dr. Powell did not acknowledge that Schwartz had never been involved with a residential development or built housing of any kind. Defendants in both matters moved to bar Dr. Powell's expert testimony on lost profits, arguing that the New Business Rule barred plaintiffs' lost profits damages claims. Both trial courts granted defendants' motion to bar Dr. Powell's expert testimony, and, therefore, both granted motions for summary judgment, dismissing the complaint with prejudice in both cases.

Plaintiffs appealed both decisions, and the Appellate Division consolidated the appeals. In agreeing with the trial court, the Appellate Division considered itself constrained to follow *Weiss* and to apply the New Business Rule as a *per se* bar against a new business' recovery for lost profits.

The Supreme Court granted plaintiffs' Petitions for Certification in which plaintiffs raised the question whether New Jersey adheres to the New Business Rule. Overruling the Appellate Division and trial court, the Supreme Court departed from *Weiss* to the extent that *Weiss* can be read to adopt a *per se* bar to all lost-profit damages claims by new businesses,

and therefore joined the majority of states that reject a bright-line rule against a new business claiming lost profits. Instead, the court reiterated the general rule under New Jersey law: "lost profits may be recoverable if they can be established with a 'reasonable degree of certainty,'" but "[a]nticipated profits that are remote, uncertain or speculative … are not recoverable." *Schwartz*, 2022 N.J. LEXIS 675, at *7. In so finding, the court noted that a majority of courts in other jurisdictions recognize that "although it is difficult for a new business to meet the standard of reasonable certainty, a *per se* ban on any claims for lost profits damages by a new business is unwarranted." *Id.* at *5.

While the court opened the door for a new business to raise a claim for lost profits, it noted that, "[i]f a new business seeks lost profits that are remote, uncertain, or speculative, the trial court should bar the evidence supporting that claim and should enter summary judgment." *Id*. at *7.

While it is now clear that New Jersey does not follow a *per se* bar on a new business claiming lost profits, the *Schwartz* decision does not necessarily give much guidance as to what New Jersey will now consider as proof of "reasonable certainty" when it comes to a new business.

Until New Jersey courts more fully develop relevant jurisprudence, New Jersey courts may look to, among other things, decisions out of Illinois and New York—both of which were specifically referenced by the court in Schwartz—for guidance.

Some examples of concepts discussed by the courts in Illinois and New York, which have permitted a new business to prove lost profits to a "reasonable degree of certainty," are the "established market analysis" and "reliance on projected sales."

In *Milex Prods., Inc. v. Alra Labs., Inc*., 603 N.E.2d 1226 (1992), the plaintiff, a contraceptive manufacturer, retained an expert to opine on its lost profits as a result of not having a new drug on the market. The expert gathered market research on two similar products in the market that were sold by competitor companies. The Appellate Court of Illinois, Second District, held that since the expert retained by the contraceptive manufacturer was "very credible," and his opinion about the contraceptive manufacturer's lost profits was based upon "actual products in the marketplace as well as authoritative sources for the data he used," the lost profit was "neither speculative nor the product of conjecture but was based upon a reasonable degree of certainty." *Id.* at 1236, 1237. The court noted that "while the product is a new one, the evidence showed it to have an established market," and ultimately affirmed the Circuit Court's judgment and the award of lost profits. *Id.* at 1237.

In *Perma Research & Dev. Co. v. Singer Co*., 402 F. Supp. 881 (S.D.N.Y. 1975), aff'd, 542 F.2d 111 (2d Cir.1976), *cert. denied*, 429 U.S. 987 (1976), an inventor of a newly patented anti-skid device sued the patent assignee for breaching a contract to market the product. The trial court found the projected sales prepared by the defendant for the device provided a rational basis for calculating the lost profits because the defendant accorded sufficient weight to the projections in deciding whether to take over the marketing of the device. *Perma Research & Dev. Co*., 402 F. Supp. at 900. In reaching that conclusion, the court noted that since profits were contemplated by the parties when they entered the contract, there is a rational basis on which to calculate the lost profits. *Id.* at 898. (Emphasis added). It should be noted, however, that since that time, the SDNY has pulled back, some, on this concept, making it clear that any calculations must be "capable of measurement based upon known reliable factors without undue speculation." *Kidder, Peabody & Co. v. IAG Int'l Acceptance Grp. N.V*., 28 F. Supp. 2d 126, 131 (S.D.N.Y. 1998). So, for example, when the expert based an opinion on the assumption of "the occurrence of numerous successive hypothetical transactions," and the party "did not have any definite or even contemplated future transactions for which any of these terms were known," the claim for damages was rejected. *Id.* at 132.

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On a going forward basis, New Jersey courts will conduct a case-specific inquiry on whether lost profits for new businesses can be established with a "reasonable degree of certainty." While there is no longer a *per se* bar to a new business recovering lost profits, if a new business seeks lost profits that are determined to be remote, uncertain, or speculative, a trial court is still to bar the evidence supporting that claim and may ultimately enter summary judgment as a result.

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