BELLSOUTH

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August 24, 1999

VIA HAND DELIVERY

David Waddell, Executive Secretary
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37238

Re: *Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*
Docket No. 98-00559 TRADD

Dear Mr. Waddell:

Enclosed are the original and thirteen copies of the Post-Hearing Brief of BellSouth Telecommunications, Inc. Copies of the enclosed are being provided to counsel of record for all parties.

Very truly yours,

Guy M. Hicks

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Enclosure

99-00210 TRADD
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BEFORE THE TENNESSEE REGULATORY AUTHORITY
Nashville, Tennessee

In Re: *Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*
Docket No. 98-00559

BellSouth Telecommunications, Inc.'s Tariff to Offer Contract Service Arrangement TN98-6766-00 for Maximum 13% Discount on Eligible Tariffed Services
Docket No. 98-00210

BellSouth Telecommunications, Inc.'s Tariff to Offer Contract Service Arrangement KY98-4958-00 for an 11% Discount on Various Services
Docket No. 98-00244

POST-HEARING BRIEF OF BELLSOUTH TELECOMMUNICATIONS, INC.

BellSouth Telecommunications Inc. ("BellSouth") respectfully submits its Post-Hearing Brief addressing the validity of the CSAs at issue in Docket No. 98-00210 (the Bank CSA) and Docket No. 98-00244 (the Store CSA). The only issues before the Tennessee Regulatory Authority ("TRA") are whether these specific CSAs comply with existing statutes and rules, and BellSouth has proven that they do. Moreover, as explained below, the Intervenors have failed to meet their burden of persuading the TRA that these two CSAs are anticompetitive or discriminatory. In particular, the Intervenors have failed to demonstrate that termination liability provisions in either these CSAs or BellSouth's tariffs are penalties, especially in light of the recent Tennessee Supreme Court decision establishing that provisions requiring a party who terminates a contract to pay the rate established in the contract for the remaining term of the contract are not penalties. The TRA, therefore, should approve both the Bank CSA and the Store CSA and allow these customers to receive the benefits for which they have bargained.

I. The only issues for consideration during the August 31, 1999 Special Conference are: (1) Whether the Bank CSA complies with existing statutes and rules; and (2) Whether the Store CSA complies with existing statutes and rules.

The "Fourth Report and Recommendation of the Pre-Hearing Officer" ("Report"), which the Directors unanimously approved during the July 13, 1999 Conference, plainly limits the issues for decision in Docket Nos. 98-00210 and 98-00244 to the approval or denial of these specific CSAs. The Report states that although the dockets addressing the Bank CSA and the Store CSA were consolidated with the Generic Docket, "the Pre-hearing Officer does not believe that individual CSAs should be contingent upon the outcome of any particular proceeding." Report at 9. The Report further states that "the nature of the relief in the two contested case dockets (the Bank CSA and the Store CSA) would be the specific approval or denial of the CSAs under consideration." Report at 15 (emphasis added).

In discussing the Intervenors' allegations of the anti-competitive effects of CSAs as a whole, the Report plainly states that "the Pre-hearing Officer is of the opinion that there would need to be a specific finding as to the specific CSAs which were indeed a part of that [allegedly anti-competitive] scheme before any CSAs could be deemed void." Report at 10 (emphasis added). The Report then plainly states that "the same reasoning would go to findings of discrimination in the offering of CSAs. The Authority would need to make a specific finding of discrimination relative to a specific CSA and not rely on a general finding of discriminatory practices in the offering of CSAs." *Id.* (emphasis added). Thus while evidence regarding CSAs in general may be relevant to a future rulemaking proceeding, it simply is not relevant to this proceeding which focuses on two specific CSAs.

II. BellSouth has met its burden of proving that the TRA should approve the Bank CSA and the Store CSA.

Rule 1220-4-1-.07 requires "public utilities" to file "special contracts between public utilities and certain customers prescribing and providing rates, services and practices not covered by or permitted in the general tariffs," and it provides that such contracts are "subject to review and approval" by the TRA. As it has done with every CSA it has entered with customers in Tennessee,[1] BellSouth filed both the Bank CSA and the Store CSA for the TRA's review and approval.[2] BellSouth also filed supporting cost information showing that each service referenced in each CSA is priced above cost even after applying the maximum discount provided in the CSA. *See* Exhibits Nos. 1 & 2. In fact, Mr. Frame testified that BellSouth reviews the price of all services referenced in every CSA to insure that the prices will remain above cost even after applying both the maximum discount provided in the CSA and the 16% discount for resold services. Tr. Vol. I.C at 143-145.

BellSouth also proved that neither the Bank nor the Store are required to purchase telecommunications services exclusively from BellSouth during the term of their respective CSAs. Vol. I.A at (37-20) to (37-21); Vol. I.D at 199. In fact, the undisputed evidence shows that other customers who have signed CSAs with BellSouth have obtained services from competitors during the term of their CSAs. Tr. Vol. I.A at 43. Moreover, the one and only CSA that is an exclusive service contract clearly states "[Customer] has requested that BellSouth serve as [Customer's] <u>exclusive provider</u> of regulated local services and intraLATA services in the BellSouth Service area . . . ." *See* Exhibit 5, ¶1 (emphasis added). The conspicuous absence of

[1] CAD witness Terry Buckner conceded that each CSA he has reviewed has been filed with and approved by the TRA. Tr. Vol. II.D at 285.

this "exclusive provider" language from the Bank CSA and the Store CSA, coupled with the undisputed evidence that other CSA customers purchase telecommunications services from competitors during the term of their CSAs, refutes any notion that these CSAs require the Bank or the Store to purchase telecommunications services only from BellSouth. Moreover, even considering these two CSAs, more than 99.9% of BellSouth's business customers have not signed a CSA with BellSouth, Tr. Vol. I.A at (37-4), and witnesses for both Nextlink and Time Warner testified that the business market in Tennessee is competitive. *See* Tr. Vol. II.B at 121 (Nextlink witness Jennifer West acknowledges that "for medium size and large customers, the market in Memphis is highly competitive."); Tr. Vol. II.A at 59 (Time Warner witness David Darrohn, testifying about contractual service arrangements, states "we use them and find them to be a useful competitive tool in a competitive marketplace.").

BellSouth also proved that neither the Bank CSA nor the Store CSA is discriminatory. BellSouth will make the terms and conditions of the Bank CSA or the Store CSA available to any similarly-situated customer who agrees to accept the terms and conditions of the CSA. Tr. Vol. I.C at 117-118; and 121. To date, however, no customer has asked to adopt the Bank CSA or the Store CSA. Vol. I.C at 117.

III. The Intervenors have not met their burden of persuasion on their claims that these individual CSAs are anticompetitive or discriminatory.

During the July 13, 1999 Director's Conference, the Directors unanimously adopted the following statement of the Pre-Hearing officer:

> As to those issues that deal with what the parties have raised in terms of discrimination and anticompetitive effects, I believe that the Intervenors would have the burden of persuasion in that area, and if they succeed with the burden of

[2]BellSouth filed the Bank CSA on March 31, 1999, and it filed the Store CSA on April 13, 1999.

> persuasion, then BellSouth would then have the burden of persuasion shifted to them to refute the allegations.

(Tr. of July 13, 1999 Conference at 21; 70-71.). As explained above, BellSouth has proven that both the Bank CSA and the Store CSA comply with applicable statutes and rules. An Intervenor seeking to challenge either of these specific CSAs, therefore, bears the burden of persuasion regarding any claim that either CSA is anticompetitive or discriminatory.

The term "burden of persuasion" typically describes "the obligation of a party to introduce evidence that persuades the factfinder, to a requisite degree of belief, that a particular proposition of fact is true," 29 Am. Jur. Evidence, §155, and a party bearing the burden of persuasion "has the burden of proving the legal elements of its case." *Id.*, §158. An Intervenor challenging either CSA, therefore, bears the burden of persuading the TRA that its challenges are firmly grounded in both fact and law. As discussed below, no Intervenor has met this burden.

A. The Intervenors have not met their burden of persuading the TRA that the termination liability provision in the Bank CSA or in the Store CSA is a penalty.

Less than two months ago, the Supreme Court of Tennessee answered the question that frequently was asked during the hearing last week: "What is a penalty under Tennessee law?" In *Guiliano v. Cleo, Inc.*, 995 S.W.2d 88, 1999 WL 439399 (July 28, 1999)(copy attached), the Supreme Court held as a matter of law that a termination liability provision is a penalty only "if the provision and the circumstances indicate that the parties intended <u>merely</u> to penalize for a breach of contract." *Cleo* at *11 (emphasis added). On the other hand, if a termination liability provision "is a reasonable estimate of the damages that would occur from a breach [of the contract], then the provision is normally construed as an enforceable stipulation of liquidated damages."[3] *Cleo* at *9. More specifically, the Supreme Court determined as a matter of law that a termination liability provision that required a party terminating a contract to pay the rate of pay established in the contract for the remaining term of the contract was <u>not</u> a penalty.

In deciding this controlling rule of law, the Supreme Court recognized that in reviewing termination liability provisions,

> there are two important interests at issue: the freedom of parties to bargain for and agree upon terms such as liquidated damages and the limitations set by public policy. Generally, the parties to a contract are free to agree upon liquidated damages and upon other terms that may not seem desirable or pleasant to outside observers. In that respect, courts should carry out the intention of the parties and the terms bargained for in the contract, unless those terms violate public policy.

Cleo at *10. The Supreme Court acknowledged that parties who agree to termination liability provisions are presumed to have "considered the certainty of liquidated damages to be preferable to the risk of proving actual damages in the event of a breach." *Cleo* at *11. The Supreme Court also acknowledged that termination liability provisions

> permit the parties to allocate business and litigation risks and often serve as part of the contractual bargain. In addition, they lend certainty to the contractual agreement and allow the parties to resolve defaults and other related disputes efficiently, when actual damages are impossible or difficult to measure.

Cleo at *11. The *Cleo* decision, therefore, is firmly grounded in sound public policy as determined by the highest Court in the State of Tennessee.

In *Cleo*, the Supreme Court considered an employment contract in which the employer agreed to hire the employee at an annual salary of $103,000 for a three-year term beginning November 1, 1992 and ending October 31, 1995. *Cleo* at *5. The contract provided that if the employer terminated the contract without cause prior to October 31, 1995, it would pay the

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[3]The term "liquidated damages" is a legal term which refers to a "sum stipulated and agreed upon by the parties at the time they enter their contract, to be paid to compensate for injuries should a breach occur." *Cleo* at *8.

employee his "then current salary from the date of termination through October 31, 1995."[4] *Cleo* at *5. The employer terminated the contract without cause in December 1994, and during that same month, the employee accepted a job with another company at an annual salary of $110,000 -- $7,000 per year more than the employee earned under the contract the employer had terminated.

The employee sought the damages set forth in the contract (his salary from December 1994 until October 31, 1995), but the employer argued that the termination liability provision was an unenforceable penalty. The employer claimed that the provision had to be construed as a penalty because it required the employer to pay the employee $90,125 plus prejudgment interest even though the employee's actual damages were far less than that amount. The Supreme Court rejected the employer's argument, ruled that the provision was not a penalty, and enforced the provision.

In reaching this decision, the Supreme Court made several important observations that are instructive on the issues before the Directors in these two specific CSA dockets. First, the Court explained that under Tennessee law,

> Courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation. Those circumstances include: whether the liquidated sum was a reasonable estimation of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract. If the provision satisfies these factors and reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages.

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[4]This provision is similar to tariffed termination liability provisions requiring a customer who signs a tariffed term contract to pay the monthly rate for the service times the number of months remaining in the term if it terminates the service early. Such provisions appear in BellSouth's tariffs, and they also appear in the local exchange tariffs of Time Warner, TCG, WorldCom, MCI Metro, and Nextlink. See Exhibit 3.

Cleo at *11. The Supreme Court then held that the termination provision that required the employer to pay the monthly salary times the number of months remaining in the contract satisfied each of these factors, explaining that:

> Neither the [employee] nor [the employer] had certain knowledge, when forming the contract, that the [employee] would be able to secure other employment in the event that [the employer] terminated his employment without cause. It was within the fair contemplation of the parties that the [employee] might not be able to find a similar professional position at the same salary and that he might suffer damages that would be difficult to prove, including loss of professional status, prestige, and advancement opportunities. The language of [the termination liability provision in the contract] reflects the parties' intentions to compensate and to protect the [employee] against these potential losses in the event of a breach by [the employer].

Cleo at *11. The Supreme Court further held that "the extent of actual damages has no bearing on the [employee's] recovery of liquidated damages under [the termination liability provision]," and it acknowledged that

> the parties themselves were in the best position to know what considerations influenced their bargaining at the time they entered into the contract. While "[t]he bargain may be an unfortunate one for the delinquent party, . . . it is not the duty of the courts of common law to relieve parties from the consequences of their own improvidence."

Cleo at *11. As the following discussion demonstrates, the Tennessee Supreme Court's most recent decision on the issue of termination liability requires a finding that the termination liability provisions in the Bank CSA and the Store CSA are not penalties.

1. The Termination Liability provision of the Store's CSA is not a penalty.

A termination liability provision is enforceable if: (1) the actual damages are indeterminable or difficult to measure at the time the contract was formed; and (2) the liquidated sum was a <u>reasonable</u> estimate of the <u>potential</u> damages that could occur upon early termination of the contract. *Cleo* at *11. As the Court of Appeals has noted, "[t]he purpose of assessing damages in a breach of contract suit is to place the plaintiff, as nearly as possible, in the same position he would have had if the contract had been performed. *Wilhite v. Brownsville Concrete Co.*, 798 S.W.2d 772, 775 (Tenn. Ct. App. 1990). Thus when an employer breaches an employment contract, the employee generally is entitled to the rate of pay set forth in the contract for the remaining term of the contract. *See, e.g., Cleo.* In addition to these damages, the party terminating the contract is generally responsible for any costs the non-breaching party incurs as a result of the breach. *See Wilhite*, 798 S.W.2d at 775 (Tenn. Ct. App. 1990)("If the defects in workmanship are so substantial that the performance of the contract made by the defendant is worthless, the contractor must pay the other party the cost of having the job redone."). Thus a termination liability provision that is reasonably related to both the costs and the damages the parties might reasonably anticipate would arise from an early termination of the contract is an enforceable liquidated damage provision, not a penalty.

a. The "cost" component of the termination liability provision in the Store CSA is not a penalty.

The costs associated with implementing and tracking a CSA are "difficult to measure." When cost issues arise in regulatory proceedings, for instance, the parties often have significantly different views of the cost associated with a particular service or element, and it is "difficult to measure" the cost that a regulatory agency will assign to a given service or element. Analogously, it is "difficult to measure" the amount of implementation or tracking costs a court or jury would determine BellSouth has incurred if the Store were to terminate its CSA.

Thus the Store and BellSouth may avoid the time, effort, and expense of having to litigate the amount of these costs in the event of an early termination of the CSA by agreeing to an amount that reasonably estimates these costs. The parties, therefore, have agreed to a formula that reasonably estimates the implementation and tracking costs to which BellSouth would be entitled upon the Store's termination of the CSA, and the parties have spelled out that formula in

Section IX of the Store CSA. *See* Exhibit 1, Amendment to Volume and Term Agreement. The "cost" component of the Store CSA's termination liability provision, therefore, satisfies the *Cleo* factors and does not constitute a penalty.

b. The "damages" component of the termination liability provision in the Store CSA is not a penalty.

The amount of damages for breach of contract that would be due upon the Store's early termination of its CSA also is difficult to measure. For example, the Store might terminate its CSA at the end of Contract Year 1. Assuming the Store met its minimum annual revenue base in Year 1, the Store reasonably could expect to pay BellSouth contract damages equal to its minimum annual revenue base for the next two years -- a total of approximately $5.5 million.[5] Even if the Store had actually billed $3 million of revenue in year 1, however, it would be required to pay only $294,682.40 under the termination liability provisions of the CSA.[6] Clearly, the termination liability amount of $294,682.40 is reasonable in relation to the actual damages of $5.5 million plus costs.

Alternatively, the Store might terminate its CSA in the eleventh month of Year 3. If the store had already exceeded its minimum annual revenue base for Year 3, BellSouth's damages would be rather low.[7] If, however, the Store is $800,000 below its minimum annual revenue

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[5]The Store's minimum annual revenue base is $2.25 million. See Exhibit 1, Section II.D.

[6]If the Store had billed $3 million of discount-eligible revenue in Year 1, it would have received $263,340 in discounts over that 12-month period. See Exhibit 1, Appendix III. Thus, under Section IX.A of the CSA, as amended, the Store would owe the discounts received for the previous 12 months ($263,340) plus prorated tracking and implementation costs of $31,342.40 (47,013.60 x 24/36). The total termination liability under the CSA, therefore, would be $294,682.40.

[7] The fact that the actual damages under this scenario would be much less than the amount due under the termination liability provision of the CSA is of no significance under the *Cleo* analysis. In *Cleo*, the Supreme Court required the employer to pay more than $90,000

base at that time, the damages are different. Under this scenario, the Store has billed $1.45 million in revenue ($2.25 million base less the $800,000 shortfall during Year 3). Assuming that all of its billing in the first eleven months of Year 3 was discount-eligible, the Store would have received $101,500 in discounts over the last eleven months.[8] Clearly, the discounts over the past twelve months plus ($101,500 plus the discounts received in the last month of Year 2) plus the pro rata implementation and tracking cost of $1,305.93 ($47,013.50 x 1/36) are reasonable in relation to BellSouth's actual damages of $800,000 plus costs. The "damages" portion of the termination liability provision in the Store's CSA, therefore, is not a penalty.

BellSouth anticipates that the Intervenors will make much of the fact that Mr. Frame did not state that the amount due under the termination liability provisions in the CSA is related to BellSouth's damages.[9] During the course of the proceeding, however, nearly every Intervenor: (1) expressly or implicitly noted that Mr. Frame was not qualified to make legal conclusions; and (2) acknowledged that what constitutes damages or penalties under contract law are legal issues.

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under the termination liability provision even though the employee was actually better off following the breach because in the same month he was terminated, he took a job with a higher annual salary. The Supreme Court expressly rejected the employer's argument that enforcing the provision under these circumstances was inappropriate, explaining that "the extent of actual damages has no bearing on the [employee's] recovery of liquidated damages . . . ." *Cleo* at *11.

[8] The discount associated with the Store's minimum annual revenue base is 7%, see Exhibit 1, Appendix III, and BellSouth applies this discount to the Store's monthly billing. See Exhibit 1, § III. The discount, therefore, would be $101,500 ($1.45 million x .07).

[9] The fact that Mr. Frame did not know the relationship between the amount set forth in the termination liability provision and breach of contract damages is neither surprising nor unique. CAD witness Terry Buckner, for example, acknowledged "I'm not a lawyer. I don't know anything about what the Court would decide in damages, the appropriate damages." Tr. Vol. II.D at 276. Similarly, CAD witness Dr. Brown testified that he does not know the amount of damages BellSouth would be entitled to recover in a breach of contract lawsuit against a customer who terminates a CSA, and he acknowledged that he therefore cannot say whether the termination liability provisions in BellSouth's CSAs are or are not related to those damages. Tr. Vol. II.D at 346-347.

For any Intervenor to now premise its legal arguments on the fact that Mr. Frame did not relate the termination liability provisions to the damages to which BellSouth would be entitled upon a breach of the CSA would be both disingenuous and erroneous.

c. The termination liability provision in the Bank's CSA is not a penalty.

As noted above, the parties could reasonably contemplate that if the Bank terminates its CSA prior to its expiration, BellSouth could recover its implementation and tracking costs (which, as explained above, are difficult to determine) and the Bank's minimum annual revenue base for the remainder of the term of the CSA. If the Bank terminates the CSA in the sixth month of the first year, therefore, BellSouth reasonably could anticipate damages of approximately $14,375,000 plus costs.[10] *See* Exhibit 2, § IX. Section IX of the Bank CSA, however, would require the Bank to pay only $3,225,000 upon such early termination.[11] Again, this amount clearly is reasonable in light of BellSouth's anticipated damages of more than $14 million.

2. The termination liability provisions in BellSouth's approved tariffs, which have the effect of law, are not penalties.

Tariffed termination liability provisions are appropriate and enforceable under the *Cleo* analysis. In fact, they have much in common with the termination liability provision the Supreme Court approved in *Cleo.* Like the contract requiring the employer to pay the terminated employee the agreed rate of pay for the remaining term of the contract, many tariffs filed by BellSouth and CLECs require a customer who terminates a term contract prior to the expiration

[10] The Bank's minimum annual revenue base in year one is $5,750,000. See Exhibit 2, Appendix II. Assuming steady monthly billing, the Bank would owe BellSouth $2,875,000 for the remainder of year 1 and $5,750,000 each for years two and three, for a total of $14,375,000.

[11] Under Section IX of the Bank CSA, the Bank would owe BellSouth $350,000 plus ($5,750,000 – 2,875,000) for a total of $3,225,000.

of the term to pay the monthly tariffed rate for the remainder of the term of the contract. Just as the employee in *Cleo* was subject to damages that would be difficult to prove in the event of a breach, many of the damages associated with an early termination of a tariffed term contract – such as implementation and tracking costs – would be difficult to prove.

Additionally, the effect of BellSouth's tariffs is much different that the effect of a commercial contract that has been neither reviewed nor approved by an agency or a court. Unlike the contract discussed in *Cleo*, BellSouth's tariffs have been approved by the appropriate regulatory agency (either the TRA or the Public Service Commission), and as the Court of Appeals has noted,

> [t]he published tariffs of a common carrier are binding upon the carrier and its customers and have the <u>effect of law</u>. The provisions of the tariffs should govern the parties.

GBM Communications, Inc. v. United Inter-Mountain Tel. Co., 723 S.W.2d 109, 112 (Tenn. Ct. App. 1986) (emphasis added). Unless and until they are amended, therefore, BellSouth's tariffed early termination penalties are lawful, and they are not penalties.[12]

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[12]During the July 13, 1999 conference, the Directors discussed the possibility of initiating a proceeding to review the termination liability provisions of BellSouth's tariffs. In determining whether to initiate such a proceeding, BellSouth respectfully submits that the Directors should consider the following facts developed during BellSouth's cross-examination of the various witnesses in this proceeding: (1) BellSouth's competitors have tariffs with substantially similar provisions; *see* Exhibit 3; (2) competitors experience the same practical, real-world difficulties winning the business of a customer who ordered services under Time Warner's tariffed four-year term as they do winning the business of a customer who has signed a tariffed term contract with BellSouth; Tr. Vol. II.B at 94; Tr. Vol. II.C at 140-141; and (3) the Consumer Advocate Division's witness Dr. Brown testified that he has the same concerns with the tariffed termination liability provisions in the Intervenors' tariffs as he has with the tariffed termination liability provisions in BellSouth's tariffs. Tr. Vol. II.D at 332-333. These facts are especially revealing in light of the fact that the TRA has not approved the tariffs of any of the Intervenors, and the Local Competition Rules describe the tariffs filed by CLECs as "informational" in nature. Local Competition Rule, 1220-4-8-.07. If the Directors decide to address tariffed termination liability provisions, BellSouth submits that the Directors should address such provisions on an industry-wide basis rather than on a piecemeal, company-by-company basis.

The termination liability provision in both the Bank CSA and the Store CSA states that it has no effect on any termination liability provisions set forth in the tariffs governing any service that is referenced in the CSA. See Exhibit 2, § IX.C; Exhibit 1, § IX.B. While the Intervenors may suggest that this provision constitutes an additional "prong" of the termination liability provision, this simply is not the case. The termination liability provisions in the CSAs and the termination liability provisions in BellSouth's tariffs are separate and distinct provisions which must be analyzed independently of one another. As Dr. Brown conceded on cross examination, a customer ordering a service under a tariffed term contract becomes subject to a termination liability provision in exchange for receiving rates that are lower that the tariffed month-to-month rates. Tr. Vol. II.D at 334-35. If that customer then signs a CSA, it becomes subject to an additional termination liability provision in exchange for receiving a further discount from the tariffed term rates. *Id.* at 335. Each termination liability provision, therefore, is reasonable in light of the damages that could be anticipated upon the termination of the document that contains the provision (i.e. the tariff or the CSA).

Moreover, as Dr. Brown conceded on cross-examination, it is entirely possible for a customer to incur a tariffed termination liability charge without incurring a CSA termination liability charge, and vice-versa. *Id.* at 336-343. A customer who terminates a tariffed term contract for ISDN services, for example, will pay the tariffed termination liability charges. If that customer still bills at least its minimum annual revenue base under the CSA, however, that customer does <u>not</u> pay termination liability charges under the CSA. Conversely, a CSA customer who orders all of its services on a month-to-month basis and terminates its CSA will pay termination liability charges under the CSA, but no tariffed termination liability charges will apply. Clearly, the tariffed termination liability provisions and the CSA termination liability provisions are separate and distinct provisions which the customer accepts in exchange for separate and distinct benefits.

Finally, the fact that one liquidated damage provision expressly or implicitly reserves a pre-existing liquidated damage provision does not convert the two valid provisions into one invalid penalty. *See Kendrick v. Alexander*, 844 S.W.2d 187, 190-191 (Tenn. Ct. App. 1992). The *Kendrick* case addressed a contract for the sale of land for $500,000. The purchasers originally gave a down payment of $10,000 which would be forfeited if they did not close on the property. The purchasers later extended the closing date by paying an addition $20,000 in earnest money which also would be forfeited if they did not close on the property. To obtain yet another extension of the closing date, the purchasers paid an addition $30,000 in earnest money which also would be forfeited if they did not close on the property. The purchasers, of course, did not close on the property, and the seller sought liquidated damages in the total amount of $60,000. Despite the fact that each liquidated amount built upon the prior amount, the Court ruled that the $60,000 liquidated damage amount was not a penalty.[13]

Revisiting the discussion of the Bank CSA's termination liability provision in Section III.A.1.C of this brief in light of the *Kendrick* analysis demonstrates that the CSAs' references to tariffed termination liability provisions does not convert the enforceable termination liability provisions into unenforceable penalties. As that section indicates, if the Bank terminates its CSA

[13] The *Kendrick* decision clearly is consistent with the *Cleo* ruling. The *Kendrick* court noted that "the fact that [the seller] ultimately sold the property for $550,000 is not determinative, as the reasonableness of a provision for liquidated damages is to be determined prospectively, i.e. at the time the parties contracted, and not retrospectively by this Court." *Kendrick*, 844 S.W.2d at 191. This is consistent with the *Cleo* decision rejecting the retrospective approach and holding that "the extent of actual damages has no bearing on the [employee's] recovery of liquidated damages under [the termination liability provisions of the contract]." *Cleo at * 11.*

in the sixth month of Year 1, the parties reasonably could anticipate damages of approximately $14,375,000 plus cost. Section IX of the Bank CSA, however, would require the Bank to pay only $3,225,000 upon early termination. Even if the Bank's termination also resulted in tariffed termination liability charges of $5,000,000, the total termination liability charges under both the CSA and the tariffs would be $8,225,000. Once again, this total amount is reasonable in relation to the reasonably anticipated damages of more than $14,000,000.

B. No Intervenor has met its burden of persuasion regarding any claims based on the cost of any service referenced by either CSA.

The CAD is the only Intervenor to present any evidence that specifically addresses the costs of any services referenced in either the Bank CSA or the Store CSA. Relying solely on the cost data filed by BellSouth, CAD witness Terry Buckner expressed concern that some of the Universal Service Ordering Codes ("USOCs") associated with some of the services referenced in the CSAs are below cost. *See* Tr. Vol. II.D at (309-38) to (309-39). BellSouth, however, has filed cost information showing that each service referenced in each CSA is priced above cost even after applying the maximum discount provided in the CSA. *See* Exhibits Nos. 1 & 2. In fact, Mr. Frame testified that BellSouth reviews the price of all services referenced in every CSA to insure that the prices will remain above cost even after applying both the maximum discount provided in the CSA and the 16% discount for resold services. Tr. Vol. I.C at 143-145. Moreover, in his rebuttal testimony, Mr. Buckner adopted the Comments attached to his testimony as Exhibit RTB-2, *see* Buckner Rebuttal at 4, and these comments state that "all the CSAs reviewed to date exceeded cost in their entirety . . . ." RTB-2 at 2 (emphasis added).

Additionally, Mr. Frame explained that "Mr. Buckner incorrectly equates individual service element or options [USOC] with a 'service,'" Tr. Vol. I.A at (37-50), and on cross examination, Mr. Buckner conceded that certain USOCs, standing alone, are no more functional that power windows standing alone. Tr. Vol. II.D at 278-80. Mr. Buckner also conceded that he "can't say" that each USOC he claims is priced below cost is, in and of itself, a functional service. Tr. Vol. II.D at 280. Clearly, the CAD has failed to carry its burden of persuading the TRA that either the Bank CSA or the Store CSA results in services that are priced below cost.

Although Time Warner suggests that the cost of some unspecified services referenced in the Bank CSA or the Store CSA may not exceed the statutory price floor for those services, it presented no evidence whatsoever regarding either the cost of any service or the price floor it contends applies to any service. Time Warner had ample opportunity to seek information related to these issues during discovery, but it chose not to do so. Time Warner also had the opportunity to present a witness who could address its assertions regarding the price floor, but it presented a witness who had never seen either of the CSAs, who had never see the cost data associated with the CSAs, and who never mentioned the statutory price floor. *See* Tr. Vol. II.B at 76-77. Having presented no evidence whatsoever in support of its price floor claims, Time Warner has failed to carry its burden of persuasion on the issue. The TRA, therefore, must reject Time Warner's suggestion that these CSAs may result in prices that could be below any price floor.

C. No Intervenor has met its burden of persuading the TRA that either the Bank CSA or the Store CSA is anticompetitive.

Although the Intervenors were on notice that the Intervenors would have the burden of persuasion" with regard to "what the parties have raised in terms of discrimination and anticompetitive effects," *See* Tr. of July 13, 1999 Conference at p. 21, the CAD was the only Intervenor to present evidence regarding these specific CSAs.[14] As CAD witness Dr. Stephen

[14] Mr. Darrohn testified that he had not reviewed either CSA, Tr. Vol. II.B at 87, and that "as far as the two specific CSAs, I don't have an opinion on [them]." Tr. Vol. II.B at 90. Ms. Brown acknowledged that her testimony did not reference either CSA, Tr. Vol. II.C at 201, and that she had not read either CSA. *Id.* at 202. Finally, Ms. West acknowledged that she did not

Brown correctly noted, however, "real conditions are the ultimate guide in sifting the many concepts that theorists can invent." *See* Tr. Vol. II.D at (314-6). Because the theories presented by the CAD's witnesses cannot pass through the sieve of the real conditions that exist with regard to these two CSAs, the CAD has failed to carry its burden of persuasion on its claims that either specific CSA is anticompetitive or discriminatory.

Much of Dr. Brown's testimony, for example, is premised on his mistaken belief that "once [BellSouth] thinks its CSA offer will be accepted by the customer, [BellSouth] takes a hardball 'take-it-or-leave-it' stance towards the customer" and forces the customer to accept terms it does not wish to accept." *See* Tr. Vol. II.D at (314-9). Mr. Frame, however, testified that these CSAs are the result of negotiations between two sophisticated business entities. Tr. Vol. I.A at (37-40); (37-5); (37-7 to 37-8). The CAD's witnesses did not refute this testimony, and they cannot refute this testimony -- both Dr. Brown and Mr. Buckner acknowledge that they had no involvement in negotiating these contracts and that they had no discussions with either the Bank or the Store regarding these CSAs. Tr. Vol. II.D at 268-69; 320. Moreover, Mr. Buckner conceded on cross-examination that "the terms of an individual CSA are, in fact, negotiated between a customer and BellSouth." Tr. Vol. II.D at 271. Dr. Brown's theory that BellSouth imposed its will on the Bank and the Store, therefore, simply does not reflect the real conditions that surrounded the negotiation of these specific CSAs.

Dr. Brown also theorizes that BellSouth insisted on the "Rate Assurance" provision in the Bank's CSA, claiming that the provision ensures that the customer will not leave BellSouth. This theory, however, overlooks the fact that this provision is conspicuously absent from the Store CSA and from the vast majority of the CSAs BellSouth has filed with the TRA. This theory also

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review either CSA and that she had never even read Mr. Frame's direct testimony which she overlooks the fact that the provision actually allows a customer to migrate services from BellSouth to a competitor and to reduce its minimum annual revenue base by a corresponding amount. *See* Exhibit 2, § XIII. Dr. Brown's theory fails to reconcile BellSouth's alleged "scheme" to ensure that the Bank will never leave BellSouth with the fact that the rate assurance provision actually accommodates the Bank's migration of services to a competitor. Finally, Dr. Brown's theory conveniently ignores Mr. Frame's undisputed testimony that: (1) the Bank requested this provision, Tr. Vol. I.A at (37-44) to (37-45); and (2) the Bank's request is not unusual given the fact that sophisticated business customers often discuss the terms and conditions of their contracts with one another. Tr. Vol. I.D at 274-78. Once again, Dr. Brown's theory regarding the rate assurance provision simply does not reflect the real conditions surrounding these negotiation of the Bank CSA.

Other theories espoused by Dr. Brown do not reflect the real conditions that exist in the Tennessee market. Dr. Brown, for instance, theorized that all 200 of BellSouth's CSAs on file with the TRA involve top 500 customers,[15] *see* Tr. Vol. II.D at 319, but the undisputed testimony reflects that only 57 of these CSAs involve top 500 customers. Tr. Vol. I.A at (37-39). Dr. Brown also theorizes that "the most likely way a tariff termination fee takes effect is when a customer switches its business to a competitor." Tr. Vol. II.D at (314-16). On cross examination, however, Dr. Brown acknowledged that he knew of no studies or other evidence which support his theory, Tr. Vol. II.D at 329, and he conceded that many reasons for a customer's termination of a tariffed service have nothing to do with the customer's desire to go to a competitor. Tr. Vol. II.D at 327-28. Moreover, while Dr. Brown theorizes that "an incumbent

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purported to rebut. Tr. Vol. II.B at 110.

[15]On cross examination, Dr. Brown acknowledged that he did not know which customers are top 500 customers. Tr. Vol. II.D at 315.

could set standing offers to beat all credible offers by entrants," Tr. Vol. II.D at (314-6), the evidence showed that Time Warner and Nextlink have their own contracts with business customers in BellSouth's service area, Tr. Vol. II.A at 59; Vol. II.B at 127, and Time Warner has more than 50 contracts with business customers in Memphis alone. *See* Exhibit 14.

Similarly, Mr. Buckner's theory that these two CSAs involve a tying arrangement has no basis in fact or law. Generally, a tying arrangement "is an agreement by a seller to sell one product (the tying product), on the condition that a buyer also purchase a second product (the tied product) from the seller." *Bell v. Cherokee Aviation Corp.*, 660 F.2d 1123, 1126 (6th Cir. 1980). As Mr. Frame explained, however, neither CSA requires the customer to order any particular product or any particular mix of products. Tr. Vol. I.D at 214-15. In fact, a customer could order one and only one service under either CSA. *Id.* Clearly, neither the Bank CSA nor the Store CSA constitutes a tying arrangement.

Moreover, Dr. Brown's theory that the business change provision of the CSAs makes the application the termination liability provisions "contingent explicitly on the customer's behavior towards [BellSouth's] competitors, period" is simply wrong. *See* Tr. Vol. II.D. at 322. Section X of the Store's CSA provides for a mutually-agreed reduction of the annual revenue base levels in the event of: (1) a divestiture of a significant part of the Store's business; (2) a "business downturn beyond [the Store's] control"; or (3) a network optimization using other BellSouth services. *See* Exhibit 1. Despite Dr. Brown's theory that the transfer of telecommunications services from BellSouth to a competitor is the only event that does not permit the Store to reduce its minimum annual revenue base, the plain language of the provision reveals otherwise. If the Store's revenue decreases because the Store makes a business decision to cut its telecommunications budget by 15%, no reduction is permitted. If the Store's revenue decreases because the store builds its own intra-company telecommunications network, no reduction is permitted. If the Store's revenue decreases because the Store decides to consolidate twenty locations into ten locations, no reduction is permitted. Clearly, this provision does not turn on the Store's actions toward competitors. Instead, it turns on the whether the reduction in revenues is a result of the store's conscious decisionmaking or events that are beyond the Store's control.

Finally, the real conditions that exist in the Tennessee telecommunications market show that Dr. Brown's concerns regarding "the ability of competitors to find customers who do not have CSAs with BellSouth" are merely cries of "wolf." *See* Tr. Vol. II.D at 348. Even considering these two specific CSAs, the undisputed proof shows that 99.9% of BellSouth's business customers (more than 199,800 of them) have not signed a CSA with BellSouth. Tr. Vol. IA at (37-4); Vol. II.D at 348-49. Clearly, these two CSAs do not inhibit the ability of BellSouth's competitors to locate and serve business customers in Tennessee.

D. No Intervenor has met its burden of proving that these particular CSAs are discriminatory.

Mr. Frame's testimony that BellSouth will make the Bank CSA or the Store CSA available to any similarly situated customer who wishes to adopt the terms and conditions of the CSA is undisputed. Tr. Vol. I.C at 117-188; 121. No Intervenor has submitted evidence showing that any customer has asked to adopt the terms and conditions of either the Bank CSA or the Store CSA. In fact, CAD witness Terry Buckner conceded on cross examination that he simply does not have enough information to say whether he believes another customer is or is not similarly situated to either the Bank or the Store. *See* Tr. Vol. II.D at 287-288. The CAD, however, conducted discovery in these and related proceedings, and BellSouth has made literally thousands of pages of information available to the CAD through discovery. If Mr. Buckner lacks sufficient information to testify whether he believes another customer is or is not similarly situated to the Bank or to the Store, it is because the CAD failed to obtain such information during discovery in this docket. The fact remains that if Mr. Buckner cannot determine that another customer is similarly situated to the Bank or the Store, he has no factual basis for his assertion that either of these individual CSAs are discriminatory, and the CAD has failed to meet its burden of persuasion on this issue.[16]

Similarly, Mr. Buckner's theory that the annual true up provision is a rebate is based on no facts whatsoever. Section 65-4-122(a) prohibits a "public service company" from using a "rebate" to collect a greater or less compensation for any service than it collects from "any other person for service of a like kind under substantially like circumstances and conditions." As noted above, neither Mr. Buckner, Dr. Brown, nor any other witness offered any testimony to show that any other customer "under substantially like circumstances and conditions" has requested to adopt either the Bank CSA or the Store CSA. The CAD, therefore, has failed to meet its burden of persuading the TRA that the true-up provision is discriminatory.

Moreover, the true-up provision is entirely appropriate. The rates charged to the Bank and the Store are based on the rates set forth in BellSouth's approved tariffs and the discounts set forth in the CSA. The true-up provision does not provide the customer with a discount above and beyond the discounts provided in the CSA. Instead, it simply ensures that the customer

[16]As noted above, the CAD bears the burden of persuading the TRA that there is, in fact, a customer who is similarly situated to the Bank or the Store and who has not been allowed to adopt the terms and conditions of the Bank's CSA or the Store's CSA. Mr. Buckner, however, merely testified that he is aware of no evidence that the CSAs are not discriminatory and that the evidence of which he is aware "is not clear enough to say that" the differences in the terms of various CSAs is due to differences in the situations of the respective customers. Tr. Vol. II.D at 287-88. Mr. Buckner's testimony that "you don't know what the mix services it (sic) is" and that "nobody knows how those discounts are arrived at", *See* Tr. Vol. II.D at 287, simply fails to meet the CAD's burden of persuasion on its claims that these specific CSAs are anticompetitive or discriminatory, especially in light of the CADs ability to determine these matters through discovery.

receives the discount to which it entitled under the contract if the customer bills more than the minimum annual revenue base it selects at the beginning of the contract year.

CONCLUSION

BellSouth filed the Bank CSA and the Store CSA under the same Rule as it has filed every other CSA the TRA has reviewed and approved, and the TRA should approve these CSAs as well. The TRA has decided to initiate a rulemaking proceeding to address CSAs on an industry-wide basis, and the decision in that rulemaking will provide guidance to the entire industry on a going-forward basis. In the meantime, the Intervenors have asked the TRA to change the manner in which it will review BellSouth's CSAs until that rulemaking is complete, while continuing to allow CLECs to enter contracts with their customers in the same manner as they always have. The approach suggested by the Intervenors clearly is self-serving, unfair, and legally deficient. The TRA, therefore, should reject that approach, approve the Bank CSA and the Store CSA, and allow the Bank and the Store to enjoy the benefits of the bargains they have negotiated.

Respectfully submitted,

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Anthony P. GUILIANO, Plaintiff/Appellant,
v.
CLEO, INC., Defendant/Appellee.

Supreme Court of Tennessee,
at Jackson.

June 28, 1999.

Executive employee of greeting card company brought action against company for breach of employment contract, alleging that company had constructively terminated his employment without cause and that he was entitled to the remainder of his salary. The Circuit Court, Shelby County, James E. Swearengen, J., granted summary judgment in favor of employee, awarding him $90,125 in salary remaining under contract, plus prejudgment interest. Company appealed. The Court of Appeals reversed damages award. Employee appealed. The Supreme Court, Barker, J., held that: (1) evidence established that employer constructively terminated marketing executive's employment without cause, thereby breaching the employment contract; (2) contract provision, stating that if employer terminated employment without cause, employee would be paid at his current salary through expiration of contract, contemplated payment of "liquidated damages" and not severance pay; (3) Tennessee adopts a prospective approach for addressing the recovery of liquidated damages, under which courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation; overruling Kimbrough & Co., 939 S.W.2d 105; Beasley v. Horrell, 864 S.W.2d 45; Kendrick v. Alexander, 844 S.W.2d 187; Harmon v. Eggers, 699 S.W.2d 159; Eller Bros. v. Home Fed. Sav. & Loan Assoc., 623 S.W.2d 624; and (4) liquidated damages provision was a reasonable estimation of potential damages at the time the parties entered into the contract, and thus was enforceable.

Court of Appeals reversed and trial court affirmed.

[1] JUDGMENT ⚿181(2)
228k181(2)
Summary judgment is appropriate only where the moving party demonstrates that there are no genuine issues of material fact and that he or she is entitled to judgment as a matter of law. Rules Civ.Proc., Rule 56.03.

[2] APPEAL AND ERROR ⚿893(1)
30k893(1)
The Supreme Court reviews a summary judgment motion as a question of law in which its inquiry is de novo without a presumption of correctness. Rules Civ.Proc., Rule 56.03.

[3] APPEAL AND ERROR ⚿934(2)
30k934(2)
In reviewing a summary judgment motion, the Supreme Court must view the evidence and all reasonable inferences in the light most favorable to the nonmoving party. Rules Civ.Proc., Rule 56.03.

[4] JUDGMENT ⚿181(2)
228k181(2)
If both the facts and conclusions to be drawn therefrom permit a reasonable person to reach only one conclusion, then summary judgment is appropriate. Rules Civ.Proc., Rule 56.03.

[5] MASTER AND SERVANT ⚿31(2)
255k31(2)
Evidence established that employer constructively terminated marketing executive's employment without cause, thereby breaching the employment contract, even though employer had right to change executive's duties, where, without showing cause to justify termination, employer demoted employee from his position as Vice President of Marketing, ordered him to stay home and wait for any future assignments, provided no such assignments, reclaimed credit cards, refused to answer telephone calls, and rescinded his authority to act on behalf of company.

[6] APPEAL AND ERROR ⚿893(1)
30k893(1)
The interpretation of a contract is a matter of law that requires a de novo review on appeal.

[7] CONTRACTS ⚿147(2)
95k147(2)
When resolving disputes concerning contract interpretation, the Supreme Court's task is to ascertain the intention of the parties based upon the usual, natural, and ordinary meaning of the contractual language.

[8] CONTRACTS ⚿143.5
95k143.5

All provisions in a contract should be construed in harmony with each other, if possible, to promote consistency and to avoid repugnancy between the various provisions of a single contract.

[9] DAMAGES 🔑78(1)
115k78(1)
Provision of employment contract, stating that if employer terminated agreement and employment without cause, employee would be paid at his current salary from date of termination through expiration of contract, contemplated payment of "liquidated damages" conditioned upon employer's breach of contract, and not severance pay, even though provision did not state that sums payable were based on an estimation of damages in the event of breach.
See publication Words and Phrases for other judicial constructions and definitions.

[9] MASTER AND SERVANT 🔑80(11)
255k80(11)
Provision of employment contract, stating that if employer terminated agreement and employment without cause, employee would be paid at his current salary from date of termination through expiration of contract, contemplated payment of "liquidated damages" conditioned upon employer's breach of contract, and not severance pay, even though provision did not state that sums payable were based on an estimation of damages in the event of breach.
See publication Words and Phrases for other judicial constructions and definitions.

[10] DAMAGES 🔑74
115k74
The term "liquidated damages" is defined by case law as a sum stipulated and agreed upon by the parties at the time they enter their contract, to be paid to compensate for injuries should a breach occur.

[11] DAMAGES 🔑74
115k74
The stipulated amount of liquidated damages represents an estimate of potential damages in the event of a contractual breach where damages are likely to be uncertain and not easily proven.

[12] MASTER AND SERVANT 🔑72
255k72
In contrast to a liquidated damages provision in an employment contract, the recovery of severance pay is not conditioned upon a breach of contract or a reasonable estimation of damages.

[13] DAMAGES 🔑78(1)
115k78(1)
A contractual provision does not have to specify a set dollar amount to constitute liquidated damages.

[14] DAMAGES 🔑78(2)
115k78(2)
A contractual provision need not explicitly include the term "liquidated damages" to constitute a liquidated damages provision.

[15] DAMAGES 🔑78(1)
115k78(1)
When a contractual provision entitles one party to a stipulated recovery following an event that constitutes a breach of contract, courts must look to the substance of the provision and the intentions of the parties to determine whether the provision calls for liquidated damages.

[16] DAMAGES 🔑78(1)
115k78(1)
If the parties agree in the contract on the amount of damages to be recovered for compensation, upon the occurrence of a particular defaulting event, then the damages are liquidated unless the contract states otherwise.

[16] DAMAGES 🔑78(2)
115k78(2)
If the parties agree in the contract on the amount of damages to be recovered for compensation, upon the occurrence of a particular defaulting event, then the damages are liquidated unless the contract states otherwise.

[17] DAMAGES 🔑76
115k76
State law disfavors the enforcement of a liquidated damages provision when the provision serves only to penalize the defaulting party for a breach of contract.

[18] DAMAGES 🔑74
115k74
As distinguished from liquidated damages, which may be enforceable, a penalty, which is not

enforceable, is a sum inserted in a contract, not as the measure of compensation for its breach, but rather as a punishment for default, or by way of security for actual damages which may be sustained by reason of nonperformance, and it involves the idea of punishment.

[19] DAMAGES ⚷74
115k74
The fundamental purpose of liquidated damages is to provide a means of compensation in the event of a breach where damages would be indeterminable or otherwise difficult to prove.

[20] DAMAGES ⚷80(1)
115k80(1)
If a contract provision is a reasonable estimate of the damages that would occur from a breach, then the provision is normally construed as an enforceable stipulation for liquidated damages; however, if the stipulated amount is unreasonable in relation to those potential or estimated damages, then it will be treated as a penalty. Restatement (Second) Contracts § 356.

[21] DAMAGES ⚷76
115k76
Generally, the parties to a contract are free to agree upon liquidated damages and upon other terms that may not seem desirable or pleasant to outside observers.

[22] CONTRACTS ⚷1
95k1
Courts should not interfere in a contract, but should carry out the intentions of the parties and the terms bargained for in the contract, unless those terms violate public policy.

[22] CONTRACTS ⚷108(1)
95k108(1)
Courts should not interfere in a contract, but should carry out the intentions of the parties and the terms bargained for in the contract, unless those terms violate public policy.

[23] DAMAGES ⚷76
115k76
Tennessee adopts a prospective approach for addressing the recovery of liquidated damages, under which courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation; overruling Kimbrough & Co., 939 S.W.2d 105; Beasley v. Horrell, 864 S.W.2d 45; Kendrick v. Alexander, 844 S.W.2d 187; Harmon, 699 S.W.2d 159; Eller Bros., Inc. v. Home Fed. Sav. & Loan Assoc., 623 S.W.2d 624.

[24] DAMAGES ⚷79(1)
115k79(1)
Circumstances considered by the court in determining the right to recover liquidated damages include whether the liquidated sum was a reasonable estimate of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract.

[24] DAMAGES ⚷80(1)
115k80(1)
Circumstances considered by the court in determining the right to recover liquidated damages include whether the liquidated sum was a reasonable estimate of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract.

[25] DAMAGES ⚷76
115k76
If a contractual provision demonstrates a reasonable estimate of potential damages, if actual damages were indeterminable or difficult to measure at the time the parties entered into the contract, and if the provision reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages; however, if the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

[25] DAMAGES ⚷79(1)
115k79(1)
If a contractual provision demonstrates a reasonable estimate of potential damages, if actual damages were indeterminable or difficult to measure at the time the parties entered into the contract, and if the provision reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages; however, if the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

[25] DAMAGES ⚿80(1)
115k80(1)
If a contractual provision demonstrates a reasonable estimate of potential damages, if actual damages were indeterminable or difficult to measure at the time the parties entered into the contract, and if the provision reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages; however, if the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

[26] DAMAGES ⚿80(1)
115k80(1)
Liquidated damages provision of employment contract, providing that employee would be paid at his current salary from date of termination through expiration of contract, was a reasonable estimation of potential damages at the time the parties entered into the contract, and thus was enforceable, even though employee secured new employment at a higher salary just after termination; it was within the fair contemplation of the parties that the employee might not be able to find a similar professional position at the same salary and that he might suffer damages that would be difficult to prove, including loss of professional status, prestige, and advancement opportunities.

[27] CONTRACTS ⚿1
95k1
While a bargain may be an unfortunate one for the delinquent party, it is not the duty of courts of common law to relieve parties from the consequences of their own improvidence.

Frank L. Watson, Waring Cox, P.L.C., Memphis, for Petitioner.

James H. Stock, Jr., Christopher E. Moore, Weintraub, Stock, Bennett, Grisham & Underwood, P.C., Memphis, for Respondent.

OPINION

BARKER, J.

***1** We granted this appeal to address the recovery of liquidated damages where a plaintiff/employee alleges that he has been constructively terminated from his employment. The trial court in this case granted summary judgment in favor of the appellant, Anthony P. Guiliano, based upon a finding that he had been constructively terminated from his employment and that he was entitled to recover the remainder of his salary under Paragraph 9 of his employment contract. [FN1] The Court of Appeals agreed that the appellant had been constructively terminated from his employment, but concluded that he was not entitled to any recovery. The intermediate court held that Paragraph 9 of the contract was a liquidated damages provision that imposed a penalty on the appellee, Cleo, Inc., (Cleo).

Both parties request this Court to determine whether Paragraph 9 of the employment contract contemplates the payment of severance pay or liquidated damages. For the reasons that follow, we conclude that the sums payable pursuant to Paragraph 9 are liquidated damages in the event that Cleo terminated appellant's employment without cause, effectively breaching the contract.

We affirm the trial court's grant of summary judgment for the appellant on the issue of constructive termination. In addition, because we find that the liquidated damages provision was a reasonable estimation of employee damages at the time the parties entered into the contract, we conclude that the appellant is entitled to recover the full amount stipulated in that provision. The judgment of the Court of Appeals is reversed, and the trial court's grant of summary judgment for the appellant is affirmed.

BACKGROUND

The essential facts in this case are undisputed. The appellant had been employed as a director of marketing at Cleo [FN2] for approximately one year when he entered into a written employment contract with the company. The contract was in the form of a letter sent by Michael Pietrangelo who was then the President and Chief Executive Officer of Cleo. The letter agreement stated in pertinent part:

> Cleo Inc. and I are very pleased that you have agreed to serve as Vice President, Marketing of Cleo Inc. (the "Company"), a wholly owned subsidiary of Gibson Greetings, Inc. As Vice President, Marketing you will report to the President, and perform those functions currently assigned, which functions and responsibilities can

be changed at the discretion of the Company. The following terms and conditions will govern your service to the Company:
1. You will serve the Company on a full-time basis as a senior executive employee, and the company will employ you as such, for a period of three years commencing November 1, 1992 and ending October 31, 1995 unless you are terminated at an earlier date pursuant to Paragraphs 6, 7, or 9 of this Agreement. Your annual salary will be $103, 000, which amount will be reviewed every fifteen months and which may be adjusted from time to time by the Company throughout the term of this Agreement in accordance with the Company's salary administration program. No later than six months prior to expiration of the original term, or any renewal term, of this Agreement, it will be reviewed by the Company for the purpose of deciding whether or not it will be renewed upon its expiration. You will be notified of a decision not to renew. If you are not notified of a decision not to renew, the Agreement will automatically renew from year to year.
***2** ....
6. In the event you are unable to perform your duties hereunder due to illness or other incapacity, which incapacity continues for more than six consecutive or nonconsecutive months in any twelve-month period, the Company shall have the right, on not less than 30 days written notice to you, to terminate this Agreement....
7. In the event you voluntarily terminate your employment during the term of this Agreement, or if the Company terminates this Agreement and your employment for cause, your right to all compensation hereunder shall cease as of the date of termination. As used in this Agreement, "cause" shall mean dishonesty, gross negligence, or willful misconduct in the performance of your duties or a willful or material breach of this Agreement. Termination of employment shall terminate this Agreement with the exception of the provisions of Paragraphs 8, 9, 10, and 12.
8. Also in the event you voluntarily terminate your employment hereunder, or in the event the Company terminates this Agreement and your employment for cause, you agree that for a period of two years after such termination, you will not compete, directly or indirectly, with the Company or with any division, subsidiary, or affiliate of the Company or participate as a director, officer, employee, consultant, advisor, partner, or joint venturer in any business engaged in the manufacture or sale of greeting cards, gift wrap, or other products produced by the Company, or any division, subsidiary, or affiliate of the Company, without the Company's prior written consent.
9. In the event the Company terminates this Agreement and your employment without cause, you shall continue to be paid your then current salary from the date of termination through October 31, 1995.

In 1994, Cleo experienced several personnel changes in its upper management. Jack Rohrbach replaced Mr. Pietrangelo as the company's President and Chief Executive Officer and Marc English was later hired as the Senior Vice President of Marketing and "Creative." Mr. Rohrbach stated in his deposition that he began observing the appellant's work performance when he took over as the company president. Based upon his observations, he opined that the appellant had a poor work relationship with his peers and subordinates and that the appellant was not leading the marketing department in a direction best suited for the company. Mr. Rohrbach stated that he hired Mr. English as the new marketing Vice President because Mr. English had more industry experience and a successful track record.

In the Fall of 1994, the appellant received a series of letters from Mr. Rohrbach and Mr. English that diminished his employment responsibilities at Cleo. The first letter, dated September 13, 1994, informed the appellant that his employment contract would not be renewed after its expiration on October 31, 1995. Approximately two weeks later, the appellant received a second letter signed by Mr. Rohrbach that stated in pertinent part:

***3** Effective today and until October 31, 1995, you are relieved of your duties as Vice President Marketing of Cleo Inc. and shall be responsible for such assignments as may be given to you by the President of the Company. During this period, you will remain an employee of the Company and the Company will continue to honor its obligations to you under your employment agreement. However, you are specifically advised that you shall have no authority to bind, represent or speak for the Company in any manner except as may be stated in writing by the President of the Company. For all future assignments, you shall be based out

of your home.
Should you accept other employment prior to October 31, 1995, all benefits under your employment agreement shall immediately cease. Also, please take note of the confidentiality and non-compete provisions of your employment agreement.
We will be in touch when an appropriate assignment becomes available. In the meantime, should you have any questions or comments, please do not hesitate to contact me.

In November, 1994, the appellant received two additional letters from Cleo informing him that he was no longer authorized to use company credit cards and that he was to return the company cards in his possession. In addition, he was informed that Cleo would no longer answer a telephone line for him. All telephone calls for the appellant were to be screened for personal or business, with the personal calls being directed to appellant's home. Cleo allowed the appellant to retrieve the personal telephone numbers from his office rolodex, but all business numbers were kept exclusively by Cleo as company property.

Following the letter of September 28, 1994, the appellant stayed at his home for three months without receiving a work assignment from Cleo. During that time, Mr. English moved into appellant's old office and assumed the marketing responsibilities previously handled by the appellant. [FN3] On December 12, 1994, the appellant accepted new employment at Wang's International, Inc. with a starting salary of $110,000 per year. Cleo kept the appellant on the company payroll at $103,000 per year until he began his new employment.

The appellant filed suit against Cleo on January 26, 1995, claiming that the company had constructively terminated his employment without cause and that he was entitled to the remainder of his salary under Paragraph 9 of the employment contract. Cleo responded that its treatment of the appellant did not constitute a termination of his employment, but that even if it did, the provision in Paragraph 9 was an unenforceable penalty. Both parties filed motions for summary judgment. After a hearing, the trial court granted summary judgment to the appellant, awarding him $90,125 in salary remaining under his employment contract plus $14,296.54 in prejudgment interest.

On appeal by Cleo, the Court of Appeals affirmed the trial court's conclusion that the appellant was constructively terminated from his employment, but reversed the award of damages. The intermediate court interpreted Paragraph 9 of the employment contract as a provision for liquidated damages because it called "for payment of a sum certain in the event of a certain occasion." Finding no evidence in the record of actual damages suffered by appellant, the court concluded that enforcement of the liquidated damages provision would impose an unlawful penalty against Cleo.

*4 The appellant requests this Court to reverse the Court of Appeals and to reinstate the judgment of the trial court. His contention in this appeal is that Cleo constructively terminated his employment when it removed his title of Vice President of Marketing and sent him home for three months without any further assignments. However, in contrast to his argument in the courts below, the appellant now claims that Cleo had a right to terminate his employment, as it did in this case, without breaching the contract. He contends that, regardless of the issue of breach, he is entitled to recover severance pay under Paragraph 9 of the employment contract.

STANDARD OF REVIEW

[1][2][3][4] The standards governing an appellate court's review of a motion for summary judgment are well settled. Summary judgment is appropriate only where the moving party demonstrates that there are no genuine issues of material fact and that he or she is entitled to judgment as a matter of law. Byrd v. Hall, 847 S.W.2d 208, 210 (Tenn.1993); Tenn. R. Civ. P. 56.03. We review the summary judgment motion as a question of law in which our inquiry is de novo without a presumption of correctness. Finister v. Humboldt Gen. Hosp., Inc., 970 S.W.2d 435, 437 (Tenn.1998); Robinson v. Omer, 952 S.W.2d 423, 426 (Tenn.1997). We must view the evidence and all reasonable inferences in the light most favorable to the nonmoving party. Byrd, 847 S.W.2d at 210- 11. If both the facts and conclusions to be drawn therefrom permit a reasonable person to reach only one conclusion, then summary judgment is appropriate. Robinson, 952 S.W.2d at 426; Bain v. Wells, 936 S.W.2d 618, 622 (Tenn.1997).

DISCUSSION

I.

[5] We shall first address whether summary judgment was appropriate on the question of constructive termination. Initially, we note that the issue of constructive termination in this case is distinguishable from cases where an at-will employee claims constructive discharge based upon a hostile work environment, discrimination, or some non-feasance on the part of the employer. See Phillips v. Interstate Hotels Corp., 974 S.W.2d 680 (Tenn.1998); Campbell v. Florida Steel Corp., 919 S.W.2d 26 (Tenn.1996). The appellant contends that Cleo removed his job title and all work responsibilities, effectively terminating his employment, without officially or formally ending the employment agreement. We view this issue strictly as one of breach of contract and conclude that the evidence clearly establishes that Cleo effectively terminated appellant's employment without cause, thereby breaching the contract.

Both the appellant and Cleo have agreed on the facts leading up to appellant's change of employment. Cleo contends, however, that it had a right to alter the appellant's work responsibilities under the employment contract, as it did in this case, without causing a termination. In support of that contention, Cleo relies on evidence that it allowed the appellant to stay on the company payroll as a senior executive employee until he obtained new employment.

*5 The resolution of this dispute centers on the construction of the employment contract. Cleo refers to that portion of the contract which states:

> Cleo Inc. and I are very pleased that you have agreed to serve as Vice President, Marketing of Cleo Inc.... As Vice President, Marketing you will report to the President, and perform those functions currently assigned, which functions and responsibilities can be changed at the discretion of the Company. The following terms and conditions will govern your service to the Company:
> 1. You will serve the Company on a full-time basis as a senior executive employee, and the Company will employ you as such, for a period of three years....

The appellant relies on the same contractual language to argue that he was employed as the Vice President of Marketing for the company. According to appellant, once Cleo removed his title and work responsibilities, it effectively ended his employment.

[6][7][8] The interpretation of a contract is a matter of law that requires a de novo review on appeal. See Hamblen County v. City of Morristown, 656 S.W.2d 331, 335-336 (Tenn.1983). When resolving disputes concerning contract interpretation, our task is to ascertain the intention of the parties based upon the usual, natural, and ordinary meaning of the contractual language. Id. at 333-34; Bob Pearsall Motors, Inc. v. Regal Chrysler-Plymouth, Inc., 521 S.W.2d 578, 580 (Tenn.1975). All provisions in the contract should be construed in harmony with each other, if possible, to promote consistency and to avoid repugnancy between the various provisions of a single contract. Rainey v. Stansell, 836 S.W.2d 117, 118-19 (Tenn.App.1992), perm. app. denied (Tenn.1992).

In this case, the contract refers to appellant's position of employment in two separate provisions. The opening provision states that he will "serve as Vice President of Marketing for Cleo, Inc.," reporting to the company president and conducting work functions that were currently assigned. The subsequent provision under Paragraph 1 describes his position as a full-time senior executive employee. We read those provisions together to mean that as Vice President of Marketing, the appellant was to be a full-time senior executive employee in the company. [FN4] Cleo promoted the appellant to that position with the condition that it could change his job functions and responsibilities during the course of the three-year contract. Those changes may have included altering his official job title. However, Cleo was contractually obligated to maintain appellant's employment as a full-time senior executive employee unless there was a cause for termination. [FN5] Cleo's contractual right to change the appellant's work duties did not include the right to remove all of his duties.

Cleo contends that it fulfilled its contractual obligation by keeping the appellant on the company payroll at his then current salary, even though it altered and effectively ended his work responsibilities. Cleo relies on the Court of Appeal's decision in Canady v. Meharry Med. College, 811 S.W.2d 902 (Tenn.App.1991), perm. app. denied (Tenn.1991). In Canady, the defendant/employer restricted the plaintiff's work duties and decided not to renew his employment contract as a hospital resident physician after the plaintiff received unsatisfactory job-performance ratings. Id. at 904. The court concluded, in part, that the restriction of plaintiff's work duties did not constitute a breach of the contract because the contract contained no express or implied assurance that the plaintiff would be given continuous, uninterrupted work assignments. Id. at 906.

***6** The circumstances in Canady are clearly distinguishable from the appellant's case. Here, we are not dealing exclusively with a change or restriction of appellant's work responsibilities. The facts are undisputed that Cleo not only demoted the appellant from his position as Vice President of Marketing, but also ordered him to stay at his home and wait for any future assignments. During the three months that the appellant stayed at home, he received no work assignments and apparently did not perform any functions on behalf of the company. In addition, Cleo reclaimed appellant's company credit cards and informed him that the company would no longer answer telephone calls for him. All business contacts for Cleo and authority to act on behalf of the company were taken away from the appellant.

The undisputed facts in this case support the lower courts' holding that the appellant was constructively terminated from his employment. Moreover, Cleo has not shown cause to justify the termination. We, therefore, conclude that summary judgment for the appellant was appropriate on that issue.

II.

[9] We shall next address whether Paragraph 9 of the employment contract provides for severance pay or liquidated damages. The appellant contends that Paragraph 9 contemplates severance pay because its payment is not specifically conditioned upon a breach of contract. Cleo argues to the contrary that the sums under Paragraph 9 are liquidated damages because that paragraph calls for the payment of a set amount in the event of a certain occasion. Cleo contends, however, that no matter what label is given to the provision, it is unenforceable because the appellant suffered no actual monetary damages.

The Court of Appeals interpreted Paragraph 9 of the employment contract as a liquidated damages provision because it contemplates the "payment of a sum certain in the event of a certain occasion." We agree that Paragraph 9 provides for liquidated damages, not severance pay. However, our interpretation of Paragraph 9 is based upon the specific contract language that recovery is due in the event that Cleo "terminates this agreement and [appellant's] employment without cause," resulting in a breach of the contract.

The distinction between liquidated damages and severance pay is important in this case. If Paragraph 9 provides for liquidated damages, then recovery is conditioned upon a showing that Cleo breached the contract and that the amount of recovery was a reasonable estimation of damages. However, if the provision calls for severance pay, then recovery by the appellant is absolute in the event of his termination, regardless of whether Cleo breached the contract or whether the amount was a reasonable damage assessment.

[10][11] The term "liquidated damages" is defined by case law as a "sum stipulated and agreed upon by the parties at the time they enter their contract, to be paid to compensate for injuries should a breach occur." V.L. Nicholson Co. v. Transcon Inv. & Fin. Ltd., Inc., 595 S.W.2d 474, 484 (Tenn.1980); Kimbrough & Co. v. Schmitt, 939 S.W.2d 105, 108 (Tenn.App.1996), perm. app. denied (Tenn.1996). The stipulated amount represents an estimate of potential damages in the event of a contractual breach where damages are likely to be uncertain and not easily proven. V.L. Nicholson, 595 S.W.2d at 484.

***7** [12] In contrast, the recovery of severance pay is not conditioned upon a breach of contract or a reasonable estimation of damages. Generally, severance pay is a form of compensation paid by an employer to an employee at a time when the employment relationship is terminated through no fault of the employee. Black's Law Dictionary 1374 (6th ed. 1990). The reason for severance pay is to offset the employee's monetary losses attributable to the dismissal from employment [FN6] and to recompense the employee for any period of time when he or she is out of work. Bradwell v. GAF Corp., 954 F.2d 798, 800 (2nd Cir.1992); 27 Am.Jur.2d Employment Relationship § 70 (1996). The amount of payment is generally based upon the types of services and the number of service years performed by the employee on behalf of the employer. See Balding v. Tennessee Dep't of Employment Sec., 212 Tenn. 517, 370 S.W.2d 546, 548 (1963).

[13] With these principles in mind, we focus on the language in Paragraph 9 to determine whether liquidated damages or severance pay was contemplated. Paragraph 9 provides that if Cleo terminates the contract and appellant's employment without cause, the appellant shall continue to receive his then current salary from the date of termination until October 31, 1995, the contract expiration date. Paragraph 9 does not state that sums payable are based upon an estimation of damages in the event of a breach of contract. However, it is clear that the provision affords the appellant a set amount of compensation in the event that Cleo terminates the agreement and appellant's employment, without cause, before the end of the contract. [FN7] Relying on the plain meaning of the language in Paragraph 9, we conclude that recovery therein is conditioned upon Cleo's breach of contract.

[14][15][16] A contractual provision need not explicitly include the term "liquidated damages" to constitute a liquidated damages provision. In cases as here, where a provision entitles one party to a stipulated recovery following an event that constitutes a breach of contract, courts must look to the substance of the provision and the intentions of the parties to determine whether the provision calls for liquidated damages. If the parties agree in the contract on the amount of damages to be recovered for compensation, upon the occurrence of a particular defaulting event, then the damages are liquidated unless the contract states otherwise. See V.L. Nicholson, 595 S.W.2d at 484.

The language in Paragraph 9 reflects the parties' intentions to compensate the appellant with a set monetary amount in the event that Cleo terminated the contract and the employment relationship without cause, before the end of the three-year term. Having further determined that the termination in this case was a breach of contract, we interpret Paragraph 9 as contemplating the payment of liquidated damages.

III.

***8** The remaining question is whether the appellant may recover any or all of the damages set forth in Paragraph 9. Under that paragraph, the sum payable is the remainder of appellant's then current salary from the date of termination until the end of the contract term on October 31, 1995. The appellant's salary as of December 1994, was $103,000. Based upon that amount and the formula provided in Paragraph 9, the trial court determined that the remainder of salary owed under the three-year contract was $90,125. [FN8]

Cleo does not dispute the calculation of damages in this case, but instead contends that the $90,125 amount plus prejudgment interest is grossly disproportional to any actual damages suffered by the appellant. Since the appellant obtained new employment on December 12, 1994, with an annual salary of $110,000, Cleo argues that appellant's recovery of liquidated damages under Paragraph 9 would constitute an unlawful penalty.

[17][18] The basis of Cleo's contention is that if the appellant suffered no actual damages from the termination of his employment, then his recovery under Paragraph 9 would have no compensatory function, but would instead simply punish Cleo for the termination. Both parties acknowledge that Tennessee law disfavors the enforcement of a liquidated damages provision when the provision serves only to penalize the defaulting party for a breach of contract. See Testerman v. Home Beneficial Life Ins. Co., 524 S.W.2d 664, 668 (Tenn.App.1974), perm. app. denied (Tenn.1975). [FN9]

[19][20] The fundamental purpose of liquidated damages is to provide a means of compensation in the event of a breach where damages would be indeterminable or otherwise difficult to prove. V.L. Nicholson, 595 S.W.2d at 484; 22 Am.Jur.2d Damages § 683 (1988); Restatement (Second) of Contracts § 356 cmt. (1979). By stipulating in the contract to the damages that might reasonably arise from a breach, the parties essentially estimate the amount of potential damages likely to be sustained by the nonbreaching party. "If the [contract] provision is a reasonable estimate of the damages that would occur from a breach, then the provision is normally construed as an enforceable stipulation for liquidated damages." V.L. Nicholson, 595 S.W.2d at 484 (citing City of Bristol v. Bostwick, 146 Tenn. 205, 240 S.W. 774 (1922); 22 Am.Jur. Damages § 227 (1965)). However, if the stipulated amount is unreasonable in relation to those potential

or estimated damages, then it will be treated as a penalty. 22 Am.Jur.2d Damages § 686 (1988); Restatement (Second) of Contracts § 356 (1979).

Although most jurisdictions disfavor the enforcement of penalties under contract law, there is a split in authority on the proper method for determining whether a liquidated damages provision constitutes a penalty. One method, commonly referred to as the "prospective approach," focuses on the estimation of potential damages and the circumstances that existed at the time of contract formation. [FN10] Under this approach, the amount of actual damages at the time of breach is of little or no significance to the recovery of liquidated damages. 22 Am.Jur.2d Damages § 723 (1988). If the liquidated sum is a reasonable prediction of potential damages and the damages are indeterminable or difficult to ascertain at the time of contract formation, then courts following the prospective approach will generally enforce the liquidated damages provision. See e.g. Gaines v. Jones, 486 F.2d 39, 46 (8th Cir.1973) (applying Missouri law); Brazen v. Bell Atl. Corp., 695 A.2d 43, 48 (Del.1997).

***9** In contrast, a second approach has developed in which courts not only analyze the estimation of damages at the time of contract formation, but also address whether the stipulated sum reasonably relates to the amount of actual damages caused by the breach. [FN11] Under this retrospective approach, the estimation of potential damages and the difficulty in measuring damages remain integral factors for the courts' review. See e.g. Lake Ridge Academy v. Carney, 66 Ohio St.3d 376, 613 N.E.2d 183, 188-89 (1993); Highgate Assoc., Ltd. v. Merryfield, 157 Vt. 313, 597 A.2d 1280, 1282 (1991). However, as part of that review, the actual damages at the time of breach are also relevant in determining whether the original estimation of damages was reasonable. See Kelly v. Marx, 44 Mass.App.Ct. 825, 694 N.E.2d 869, 871 (1998); Wassenaar v. Panos, 111 Wis.2d 518, 331 N.W.2d 357, 361-62 (1983). If the liquidated sum greatly exceeds the amount of actual damages, then courts following this latter approach will treat the estimated sum as a penalty and will limit recovery to the actual damages. Kelly, 694 N.E.2d at 871; Shallow Brook Assoc. v. Dube, 135 N.H. 40, 599 A.2d 132, 137 (1991).

While this Court has not previously addressed the issue, we note that the Court of Appeals has followed the latter approach using both a prospective review of the circumstances at the time of contract formation and a review of the actual damages at the time of breach. See Kimbrough & Co., 939 S.W.2d at 108; Beasley v. Horrell, 864 S.W.2d 45, 50 (Tenn.App.1993), perm. app. denied (Tenn.1993); Kendrick v. Alexander, 844 S.W.2d 187, 190-91 (Tenn.App.1992), perm. app. denied (Tenn.1992) (following a prospective approach for assessing the reasonableness of a liquidated damages provision); Harmon, 699 S.W.2d at 163; Eller Bros., Inc. v. Home Fed. Sav. & Loan Assoc., 623 S.W.2d 624, 628 (Tenn.App.1981), perm. app. denied (Tenn.1981). After careful consideration, we find that there are inherent problems with the retrospective analysis and are persuaded that a prospective approach is the better rule. Therefore, to the extent that the Court of Appeals has adopted a retrospective approach, as reflected in Eller Bros., Harmon, Beasley, and Kimbrough & Co., that approach is overruled.

[21][22] From our review of the law on liquidated damages, we recognize that there are two important interests at issue: the freedom of parties to bargain for and to agree upon terms such as liquidated damages and the limitations set by public policy. Generally, the parties to a contract are free to agree upon liquidated damages and upon other terms that may not seem desirable or pleasant to outside observers. See Chapman Drug Co. v. Chapman, 207 Tenn. 502, 341 S.W.2d 392, 398 (1960); 22 Am.Jur.2d Damages § 686 (1988). In that respect, courts should not interfere in the contract, but should carry out the intentions of the parties and the terms bargained for in the contract, unless those terms violate public policy. See McKay v. Louisville & N.R. Co., 133 Tenn. 590, 182 S.W. 874, 875 (1916) (citing Baltimore & Ohio S.W. Ry. Co. v. Voight, 176 U.S. 498, 505, 20 S.Ct. 385, 387, 44 L.Ed. 560 (1900)).

***10** Both the prospective and the retrospective approaches allow courts to review liquidated damages provisions together with the limitations set by public policy. However, we conclude that the prospective approach is the better rule based upon the consideration it affords to the intentions of the parties and to the freedom to contract.

When parties agree to a liquidated damages provision, it is generally presumed that they considered the certainty of liquidated damages to be preferable to the risk of proving actual damages in the event of a breach. 22 Am.Jur.2d Damages § 726.

Liquidated damages permit the parties to allocate business and litigation risks and often serve as part of the contractual bargain. In addition, they lend certainty to the contractual agreement and allow the parties to resolve defaults and other related disputes efficiently, when actual damages are impossible or difficult to measure. C.T. McCormick, Handbook on the Law of Damages § 157 (1935).

The retrospective approach, however, undermines the certainty and other benefits afforded by liquidated damages. Under that approach, the parties are allowed to fully litigate actual damages following a breach of contract. If the nonbreaching party fails to prove actual damages, then he or she is barred from recovering the liquidated sum originally agreed upon in the contract. We find that it is unfair to require the nonbreaching party to prove actual damages in cases where the parties agreed in advance to a liquidated damages provision. Such a requirement ignores the original intentions of the parties and defeats the purposes of stipulating in advance to potential damages.

[23][24][25] We, therefore, adopt a prospective approach for addressing the recovery of liquidated damages. Under this approach, courts must focus on the intentions of the parties based upon the language in the contract and the circumstances that existed at the time of contract formation. [FN12] Those circumstances include: whether the liquidated sum was a reasonable estimate of potential damages and whether actual damages were indeterminable or difficult to measure at the time the parties entered into the contract. See V.L. Nicholson, 595 S.W.2d at 484. If the provision satisfies those factors and reflects the parties' intentions to compensate in the event of a breach, then the provision will be upheld as a reasonable agreement for liquidated damages. However, if the provision and circumstances indicate that the parties intended merely to penalize for a breach of contract, then the provision is unenforceable as against public policy.

IV.

[26] We now turn to the liquidated damages provision in this case. The Court of Appeals found that the liquidated sum was a reasonable estimation of potential damages at the time the parties entered into the contract. We agree. Neither the appellant nor Cleo had certain knowledge, when forming the contract, that the appellant would be able to secure other employment in the event that Cleo terminated his employment without cause. It was within the fair contemplation of the parties that the appellant might not be able to find a similar professional position at the same salary and that he might suffer damages that would be difficult to prove, including loss of professional status, prestige, and advancement opportunities. The language in Paragraph 9 reflects the parties' intentions to compensate and to protect the appellant against those potential losses in the event of a breach by Cleo.

***11** The Court of Appeals, however, went further in addressing whether the stipulated sum reasonably related to the appellant's actual damages. Cleo insists that the intermediate court's analysis was both proper and fair based upon the fact that the appellant obtained new employment at a higher salary after the termination. While we question whether the record is sufficient on the issue of actual damages, [FN13] we conclude that the extent of actual damages has no bearing on the appellant's recovery of liquidated damages under Paragraph 9. The liquidated sum is recoverable based upon our conclusion that it was reasonable at the time the parties entered into the contract and that it reflects the parties' original intentions to compensate for a termination of employment.

[27] The parties themselves were in the best position to know what considerations influenced their bargaining at the time they entered into the contract. While " '[t]he bargain may be an unfortunate one for the delinquent party, ... it is not the duty of courts of common law to relieve parties from the consequences of their own improvidence.' " Watson v. Ingram, 124 Wash.2d 845, 881 P.2d 247, 250 (1994) (quoting Dwinel v. Brown, 54 Me. 468, 470 (1867)). See also McKay, 182 S.W. at 875; Whaley v. Underwood, 922 S.W.2d 110, 112 (Tenn.App.1995). Accordingly, to the extent the Court of Appeals based its decision upon a review of actual damages, that decision is overruled.

CONCLUSION

Based upon the foregoing, we conclude that summary judgment for the appellant was appropriate on the issue of constructive termination. Moreover, because Paragraph 9 was a reasonable estimation of damages at the time the parties entered into the contract, we conclude that the appellant is entitled to recover the full amount stipulated in that provision. The judgment of the Court of Appeals is reversed and the trial court's award of summary judgment for the appellant is reinstated. Costs of this appeal are taxed to the appellee, Cleo.

ANDERSON, C.J., and DROWOTA, BIRCH, HOLDER, JJ.

FN1. The trial court awarded $90,125 in back salary plus $14,296.54 in prejudgment interest, for a total award of $104,421.54. The record is unclear whether the trial court treated that recovery as severance pay or liquidated damages.

FN2. At all times relevant to this case, Cleo was a wholly owned subsidiary of Gibson Greetings, Inc.

FN3. Mr. Rohrbach stated in his deposition that Mr. English took on other responsibilities at Cleo in addition to those previously handled by the appellant.

FN4. The Court of Appeals determined that the appellant was employed exclusively as the Vice President of Marketing based upon the opening provision of the employment contract. The court held that to the extent the subsequent provisions described the appellant as a senior executive employee, those latter provisions were unenforceable as being in conflict with the preceding "Vice President of Marketing" provision. We hold to the contrary that the provisions can be read congruently without having to redact any portion of the contract.

FN5. As previously mentioned, "cause" was defined in the contract as "dishonesty, gross negligence, or willful misconduct in the performance of work duties or a willful or material breach of [the employment] Agreement." Cleo also had a right to terminate the contract under certain conditions of illness or incapacity as defined in Paragraph 6 of the contract.

FN6. Those losses may include seniority rights, pension recovery, and re- training costs or other burdens associated with obtaining new employment.

FN7. The appellant argues, in part, that the dollar amount established in Paragraph 9 cannot be construed as liquidated damages because it is not sufficiently definite to constitute a "sum certain." We afford no merit to this contention. Under Tennessee law, a contractual provision does not have to specify a set dollar amount to constitute liquidated damages. See Vanderbilt Univ. v. DiNardo, 974 F.Supp. 638, 640 (M.D.Tenn.1997) (applying Tennessee law), rev'd in part, 174 F.3d 751(6th Cir. 1999) (upholding the liquidated damages provision, but remanding for trial on a contract addendum); Harmon v. Eggers, 699 S.W.2d 159, 160 (Tenn.Ct.App.1985), perm. app. denied (Tenn.1985).

FN8. The record does not reflect the exact date found by the trial court as the date when appellant was terminated from his employment. However, based upon the $90,125 amount, it is apparent that the trial court treated December 15, 1994, as the approximate date of termination. That date coincides with a letter sent by Cleo to the appellant on December 22, 1994, stating that the appellant had been paid his employment wages through December 15, 1994.

FN9. As distinguished from liquidated damages, a penalty is "a sum inserted in a contract, not as the measure of compensation for its breach, but rather as a punishment for default, or by way of security for actual damages which may be sustained by reason of nonperformance, and it involves the idea of punishment." 22 Am.Jur.2d Damages § 684 (1988).

FN10. See United States v. Bethlehem Steel Co., 205 U.S. 105, 119, 27 S.Ct. 450, 455, 51 L.Ed. 731 (1907); Gaines v. Jones, 486 F.2d 39, 44- 45 (8th Cir.1973); United States v. Le Roy Dyal Co., 186 F.2d 460, 462 (3rd Cir.1950); Williwaw Lodge v. Locke, 601 P.2d 236, 239 (Alaska 1979); Omohundro v. Ottenheimer, 198 Ark. 137, 127 S.W.2d 642, 645 (1939); McCarthy v. Tally, 46 Cal.2d 577, 297 P.2d 981, 986-87 (1956) (in banc); Rohauer v. Little, 736 P.2d 403, 410 (Colo.1987); Hanson Dev. Co. v. East Great Plains Shopping Ctr., Inc., 195 Conn. 60, 485 A.2d 1296, 1300 (1985); Brazen v. Bell Atl. Corp., 695 A.2d 43, 48 (Del.1997); Lefemine v. Baron, 573 So.2d 326, 328 (Fla.1991); Fickling & Walker Co. v. Giddens Constr. Co., 258 Ga. 891, 376 S.E.2d 655, 659-60 (1989); Anne Arundel County v. Norair Engr. Corp., 275 Md. 480, 341

A.2d 287, 294 (1975); Frank v. Jansen, 303 Minn. 86, 226 N.W.2d 739 (1975); Board of Trustees of State Inst. of Higher Learning v. Johnson, 507 So.2d 887, 890 (Miss.1987); Knutton v. Cofield, 273 N.C. 355, 160 S.E.2d 29, 35-36 (1968); Fisher v. Schmeling, 520 N.W.2d 820, 822 (N.D.1994); Safari, Inc. v. Verdoorn, 446 N.W.2d 44, 46 (S.D.1989); Woodhaven Apartments v. Washington, 942 P.2d 918, 921 (Utah 1997).

FN11. See Thanksgiving Tower Partners v. Anros Thanksgiving Partners, 64 F.3d 227, 232 (5th Cir.1995) (applying Texas law); Southpace Properties, Inc. v. Acquisition Group, 5 F.3d 500, 505 (11th Cir.1993) (applying Alabama law); Kelly v. Marx, 44 Mass.App.Ct. 825, 694 N.E.2d 869, 871-72 (1998); Hawkins v. Foster, 897 S.W.2d 80, 85 (Mo.Ct.App.1995); Browning Ferris Indus. of Nebraska, Inc. v. Eating Establishment 90th & Fort, Inc., 6 Neb.App. 608, 575 N.W.2d 885, 888-89 (1998); Shallow Brook Assoc. v. Dube, 135 N.H. 40, 599 A.2d 132, 137 (1991); Boyle v. Petrie Stores Corp., 136 Misc.2d 380, 518 N.Y.S.2d 854, 861 (N.Y.Sup.Ct.1985), supp. decision (May 29, 1987); Lake Ridge Academy v. Carney, 66 Ohio St.3d 376, 613 N.E.2d 183, 189 (Ohio 1993); Highgate Assoc., Ltd. v. Merryfield, 157 Vt. 313, 597 A.2d 1280, 1282 (1991) (reviewing the totality of the circumstances); Wheeling Clinic v. Van Pelt, 192 W.Va. 620, 453 S.E.2d 603, 609 (1994); Wassenaar v. Panos, 111 Wis.2d 518, 331 N.W.2d 357, 361-62 (1983) (reviewing the totality of the circumstances, including actual damages).

FN12. This prospective approach incorporates the cardinal rule of contract interpretation, requiring courts to ascertain the intentions of the parties based upon the language in the contract. See Bob Pearsall Motors, Inc., 521 S.W.2d at 580; Nunnelly v. Warner Iron Co., 94 Tenn. 282, 29 S.W. 124 (1895).

FN13. The trial court awarded summary judgment to the appellant without making a finding on actual damages or whether the recovery constituted severance pay or liquidated damages. Nevertheless, because we hold that actual damages are immaterial in this case, we need not address the sufficiency of the record in that respect.

END OF DOCUMENT

CERTIFICATE OF SERVICE

I hereby certify that on August 24, 1999, a copy of the foregoing document was served on the parties of record, via the method indicated:

[✓] Hand [ ] Mail [ ] Facsimile [ ] Overnight	Richard Collier, Esquire Tennessee Regulatory Authority 460 James Robertson Parkway Nashville, TN 37243-0500
[ ] Hand [ ] Mail [✓] Facsimile [ ] Overnight	Henry Walker, Esquire Boult, Cummings, et al. 414 Union Ave., #1600 P. O. Box 198062 Nashville, TN 39219-8062
[ ] Hand [ ] Mail [✓] Facsimile [ ] Overnight	Jon Hastings, Esquire Boult, Cummings, et al. 414 Union St., #1600 Nashville, TN 37219
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