

## *Hadley v Baxendale*

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### ***Introduction and Frank Guest***

Although Frank Guest died nearly seven years before I was born, I am delighted and greatly honoured to deliver this lecture in his honour. One of the reasons for my delight is my enduring belief in his vision and legacy for legal education. He was, of course, an extremely esteemed academic lawyer. He was the first Chair of Law at the University of Otago, the first full-time Dean of Law, and the founder of the Otago Law Review. But most fundamentally for the purposes of this lecture, he steered the Faculty of Law by treating legal education, and the academic branch of the legal profession, as working in harmony with the practising branch and the judiciary. He was a trained philosopher but also deeply attuned to the practice of law. Indeed, he served a term as the President of the Otago District Law Society. In Donald McRae’s reflections on the origins of the Otago Law Review in 2015, he described how, in Professor Guest’s time, law classes were held in locations including the second floor of the Supreme Court building on Lower Stuart Street. The members of the profession were well known to the students. Many of them were lecturers. A similar story can be told of many of the leading law schools in Australia. From all accounts, Frank Guest was a brilliant teacher who realised the power of a close association between academia and the judiciary.

I cannot speak of the relationship in New Zealand between the academy and the other branches of the profession but, in Australia, the relations are no longer so close. It is

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\* Although this article is written in my voice, Ms Bourke’s outstanding assistance with research and with discussion of the ideas justifies the article being expressed as jointly authored.

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sometimes said that courts are not assisted by a detailed academic focus, such as upon history or theory, to resolve legal problems. Even worse, on occasion ‘academic’ can be used as a term of derision. From an intensely realist perspective of law these views might be understandable. For instance, in reporting an interview with Richard Posner on his retirement, the *New York Times* related that he said that as a judge, “The first thing you do is ask yourself — forget about the law — what is a sensible resolution of this dispute?” Then, he apparently said that his next step was to see if a recent Supreme Court precedent or some other legal obstacle stood in the way of ruling in favour of that sensible resolution. “And the answer is that’s actually rarely the case,” he said. “When you have a Supreme Court case or something similar, they’re often extremely easy to get around.”<sup>1</sup>

A different view is that history, precedent, and theory are aspects that make up what Frederick Pollock described as the “science” of the law,<sup>2</sup> rather than mere obstacles to be navigated as simply and sharply as possible in the course of making a ruling that appeals to the particular judge. One of the sources of my great pleasure in delivering the lecture this evening is that, like Frank Guest, I am not a realist in the Posnerian sense. Although the law is socially constructed, it is a social science. And in its scientific method, involving a pathway, in the words of Ronald Dworkin echoing Lord Mansfield, to “work[ ] itself pure”,<sup>3</sup> it has commonalities with the natural sciences.

My lecture tonight in honour of Frank Guest is a salutary tale of the importance of a harmonious operation between the academy and the other branches of the profession. It is tale of a decision, 150 years ago, which borrowed heavily, but without attribution, from academic work. It is a tale of a decision which, shorn from its academic roots, was of poor quality but which was lionised and lauded despite reasoning which barely touched upon the difficult underlying controversies. Those controversies, again through academic writing, have only recently been exposed in England. Although my focus is heavily upon the English academic and judicial treatment of this decision, as Professor Ahdar of this University has pointed out, the modern difficulties with the decision were seen by Sir Robin Cooke nearly three decades earlier.<sup>4</sup> It might fairly be said that, like pavlova and Russell Crowe, New Zealand has first claim. The decision about which I speak is, of course, *Hadley v Baxendale*.

### ***Hadley v Baxendale***

In 1866, Pollock CB said of *Hadley v Baxendale*<sup>5</sup> that:<sup>6</sup>

... a more extensive and accurate knowledge of decisions in our law books, and a more accurate power of analyzing and discussing them, and ... a larger acquaintance with the exigencies of commerce and the business of life, never combined to assist at the formation of any decision.

It was a significant influence in the drafting of the Sale of Goods Act 1893 (UK),<sup>7</sup> in s 73 of the Indian Contract Act 1872,<sup>8</sup> and possibly in the drafting of the Vienna Convention on the

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<sup>1</sup> A Liptak “An Exit Interview With Richard Posner, Judicial Provocateur” *The New York Times* (online ed, New York, 11 September 2017).

<sup>2</sup> F Pollock “Essays in Jurisprudence and Ethics” (Macmillan and Co, London, 1882) at ch 1 and ch 9.

<sup>3</sup> R Dworkin “Law’s Ambition for Itself” (1985) 71 *Va L Rev* 173 at 173.

<sup>4</sup> R Cooke “Remoteness of Damages and Judicial Discretion” (1978) 37 *Camb LJ* 288; *McElroy Milne v Commercial Electronics Ltd* [1993] 1 *NZLR* 39 (CA). See R Ahdar “Remoteness, ‘Ritual Incarnation’ and the Future of *Hadley v Baxendale*: Reflections from New Zealand” (1994) 7 *JCL* 53.

<sup>5</sup> *Hadley v Baxendale* (1854) 9 *Ex* 341, 156 *ER* 145 (Exch).

<sup>6</sup> *Wilson v The Newport Dock Company* (1866) *LR* 1 *Ex* 177 (Exch) at 189.

<sup>7</sup> Sale of Goods Act 1893 (UK) 56 & 57 *Vict c* 71.

International Sale of Goods.<sup>9</sup> By 1951, Corbin described the decision as “more often cited as authority than any other case in the law of damages”.<sup>10</sup> And in 2001, Murray said that the principle had been “universally accepted” by courts in the United States as a correct statement of the principle concerning the extent of recovery in an action for breach of contract.<sup>11</sup> Such is the importance of *Hadley v Baxendale* that songs have been written about it,<sup>12</sup> and a conference was held in 2004 to celebrate its 150<sup>th</sup> anniversary.<sup>13</sup> *Hadley v Baxendale* is usually described as a revolutionary case concerning damages for breach of contract, reflected in a brilliant decision. This common understanding makes three errors. First, it was not revolutionary. Secondly, it was not a case about breach of contract. Thirdly, the case was probably wrongly decided. Nevertheless, the decision has had an enormous influence on the development of rules concerning the law of damages and it is a powerful illustration of the need for all branches of the legal profession to work together.

### ***The lack of novelty of Hadley v Baxendale***

Let me start with the roots of the decision in *Hadley v Baxendale*. The rule set out in *Hadley v Baxendale* was not novel. The need for limits upon recoverability of damages was well known to the Romans. It was important in the approach taken by Paul to the *Lex Aquilia*.<sup>14</sup> In 1546, the French jurist Charles Dumoulin, relying upon a constitution of Justinian, argued that the basis for the principle was that liability for breach of contract should be limited only to damage that could be foreseen by the breaching party.<sup>15</sup> Then, in 1806, Dumoulin’s test was referred to by Pothier in his *Treatise on the Law of Obligations or Contracts*; half a century prior to the decision in *Hadley v Baxendale*. Pothier expressed the test as follows:<sup>16</sup>

When the debtor cannot be charged with any fraud, and is merely in fault for not performing his obligation, ... the debtor is only liable for the damages and interest which might have been contemplated at the time of the contract; for to such alone the debtor can be considered as having intended to submit.

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<sup>8</sup> Indian Contract Act 1872 (India), s 73. See the editor’s note to FE Smith “The Rule in *Hadley v. Baxendale*” (1900) 16 LQR 275 at 287. See also L Stephen *The Life of Sir James Fitzjames Stephen: A Judge of the High Court of Justice* (GP Putnam’s Sons, New York, 1895; Smith, Elder, & Co, London, 1895).

<sup>9</sup> United Nations Convention on Contracts for the International Sale of Goods 1489 UNTS 3 (opened for signature 11 April 1980, entered into force 1 January 1988). See F Ferrari “Comparative Ruminations on the Foreseeability of Damages in Contract Law” (1993) 53 La L Rev 1257 at 1262; AG Murphey Jr “Consequential Damages in Contracts for the International Sale of Goods and the Legacy of *Hadley*” (1989) 23 Geo Wash J Int’l L & Econ 415. See also KS Cohen “Achieving a Uniform Law Governing International Sales: Conforming the Damages Provisions of the United Nations Convention on Contracts for the International Sale of Goods and the Uniform Commercial Code” (2005) 26 U Pa J Int’l Econ L 601 at 611; U Magnus *Wiener UN-Kaufrecht – CISG* (Sellier-de Gruyter, Berlin, 2005) at 171 (translation: *UN: CISG; the Vienna Convention*); JM West and JKM Ohnesorge “The 1980 UN Convention on Contracts for the International Sale of Goods: A Comparative Analysis of Consequences of Accession by the Republic of Korea” (1999) 12 Transnat’l Law 63 at 97.

<sup>10</sup> AL Corbin *Corbin on Contracts* (West Publishing Co, St Paul (Minn), 1951) at 5 and 93.

<sup>11</sup> JE Murray Jr *Murray on Contracts* (4th ed, Newark, LexisNexis, 2001) at 784 [§ 120(A)].

<sup>12</sup> See FG Snyder “The Shaft: The *Hadley v. Baxendale* Song” (2005) 11 Tex Wesleyan L Rev 239.

<sup>13</sup> The Common Law of Contracts as a World Force in Two Ages of Revolution: A Conference Celebrating the 150th Anniversary of *Hadley v. Baxendale*, papers published in (2005) 11 Tex Wesleyan L Rev at 225–725.

<sup>14</sup> Digest of Justinian, 9.2.28 and 9.2.31 (translated ed: CH Monro (translator) *The Digest of Justinian* (Cambridge University Press, Cambridge, 1904) vol 2 at 131 and 134). See H Scott “Pits and Pruners: *Culpa* and Social Practice in Digest 9.2” in A Burrows, D Johnston and R Zimmermann (eds) *Judge and Jurist: Essays in Memory of Lord Rodger of Earlsferry* (Oxford University Press, Oxford, 2013) at ch 23.

<sup>15</sup> C Dumoulin *Tractatus Commerciorum et Usurarum* (1546) (translation: *Treatise on Contracts and Usury*).

<sup>16</sup> RJ Pothier *Traité des Obligations* (Orléans, 1761) (translated ed: WD Evans (translator) RJ Pothier *A Treatise on the Law of Obligations or Contracts* (London, 1806) vol 1 at pt 1, ch 2, art 3, [160]).

A similar rule was incorporated in the Italian Civil Code, the Belgian Civil Code and the Louisiana Civil Code.<sup>17</sup> The rule soon crossed into United States common law in the Supreme Court of Judicature of New York<sup>18</sup> and appeared in the first and second editions of Sedgwick's American treatise,<sup>19</sup> and in Kent's *Commentaries on American Law*.<sup>20</sup> By 1854, when the Court of Exchequer heard *Hadley v Baxendale*, the rule was well established outside England.

### ***The English position prior to Hadley v Baxendale***

Prior to *Hadley v Baxendale*, the rules concerning damages in England were, in large part, more generous than the civilian law. The apogee of the older English approach might be summed up in the decision of Parke B in *Robinson v Harman*, that:<sup>21</sup>

... where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.

As Washington described this statement in 1932, it was one which, though once fully accepted, "has become one of those generous aspirations which the law does well to put but sparingly into practice".<sup>22</sup> The brakes on full compensation as generously described in *Robinson v Harman* were generally hidden. When *Hadley v Baxendale* was decided there were very few judges sitting in superior courts and the vast majority of civil disputes were heard in the county courts by judges sitting with juries.<sup>23</sup> The calculation of damages had been generally left up to discretion of juries, without judicial guidance<sup>24</sup> and one can surmise that juries used their discretion as a practical brake on unlimited damages.

Although, prior to *Hadley v Baxendale* there had been hints of a restraining rule of remoteness,<sup>25</sup> a limiting principle upon damages was far from established. Indeed, two cases before the Court of Exchequer just before *Hadley v Baxendale* seemed to leave the whole question to the jury's discretion. The first case, *Black v Baxendale* – involving the same Baxendale as in *Hadley v Baxendale* – involved a defendant who was two days late in

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<sup>17</sup> Italian Civil Code, art 1225 as cited in F Ferrari "*Hadley v Baxendale* v Foreseeability under Article 74 CISG" in D Saidov and R Cunnington (eds) *Contract Damages: Domestic and International Perspectives* (Hart Publishing, Oxford, 2008) 305 at 318 ("Unless the non-performance or the delay depends on the debtor's fraud, the compensation is limited to the damages which could be foreseen at the time when the obligation came into existence"); Belgian Civil Code, art 1150; Louisiana Civil Code, art 1996 ("An obligor in good faith is liable only for the damages that were foreseeable at the time the contract was made").

<sup>18</sup> *Blanchard v Ely* 21 Wend 342 (NY 1839).

<sup>19</sup> T Sedgwick *A Treatise on the Measure of Damages* (John S Voorhies, New York, 1847); T Sedgwick *A Treatise on the Measure of Damages* (2nd ed, John S Voorhies, New York, 1852).

<sup>20</sup> J Kent *Commentaries on American Law* (10th ed, Little, Brown and Company, Boston, 1860) vol 2 at 665. Kent explained that "[d]amages for breach of contract are only those which are incidental to, and directly caused by, the breach, and may reasonably be supposed to have entered into the contemplation of the parties, and not speculative profits, or accidental or consequential losses".

<sup>21</sup> *Robinson v Harman* (1848) 1 Ex 850 at 855, 154 ER 363 (Exch) at 365.

<sup>22</sup> GT Washington "Damages in Contract at Common Law II: The Period Transitional to the Modern Law" (1932) 48 LQR 90 at 107.

<sup>23</sup> R Danzig "Hadley v. Baxendale: A Study in the Industrialization of the Law" (1975) 4 JLS 249 at 270.

<sup>24</sup> At 255.

<sup>25</sup> In *Boorman v Nash* (1829) 9 B & C 145 at 152, 109 ER 54 (Exch) at 57 damages were described as being awarded because they "necessarily resulted from the ... breach". In *Walton v Fothergill* (1835) 7 C & P 392 at 394, 173 ER 174 (Comm Pleas) at 175, damages were awarded for "necessary and natural consequences" of the breach.

delivering five bundles of haycloths.<sup>26</sup> Three of the four judges who decided *Hadley v Baxendale* were involved in the case: Alderson and Parke BB were judges, and Martin B was Baxendale's counsel. At trial in *Black v Baxendale*, the Court left it to the jury to determine whether the expenses incurred as a result of the delayed delivery were reasonable.<sup>27</sup> The jury awarded damages for lost profits. Baxendale appealed. Contrary to what he would later hold in *Hadley v Baxendale*, Alderson B said, "Whether these expenses were reasonable was entirely a question for the jury."<sup>28</sup> For this reason, the Court of Exchequer refused to grant a new trial.<sup>29</sup> Pollock CB said:<sup>30</sup>

The jury were wrong in giving too large an amount of damages. If the carriers had had distinct notice that the goods would be required to be delivered at a particular time, perhaps they would have been liable for those expenses, for which, without such notice, they would not otherwise be liable; but whether any particular class of expenses is reasonable or not depends upon the usage of trade, and various other circumstances. It is not a question for the Judge, but for the jury, to decide what are reasonable expenses.

The second case was *Waters v Towers*,<sup>31</sup> decided one year before *Hadley v Baxendale*. Waters claimed that Towers had not completed work on Waters' mill within a reasonable time nor fitted it in a workmanlike manner. Waters claimed for loss of profits. Relying on the contemplation rule in Kent's *Commentaries*,<sup>32</sup> Towers submitted that the loss of profits was too remote. Pollock CB and Alderson and Martin BB found for Waters without giving reasons. The identical panel of judges, after reasons given one year later in *Hadley v Baxendale*, might have decided the case differently.

### ***The facts of Hadley v Baxendale***

Joseph and Jonah Hadley conducted a business cleaning corn, grounding the corn into meal, and dressing it into flour, sharps and bran. They used a steam engine in the process.<sup>33</sup> When the steam engine's crank shaft broke, they ordered a new one from engineers W Joyce & Co in Greenwich. The engineers needed the broken crank shaft so that the new shaft could be designed to fit the steam engine. The Hadleys engaged Pickford & Co as common carriers to deliver the crank shaft to the engineers.<sup>34</sup> The Hadleys paid 2l 4s for the delivery, with one of the Hadleys' employees telling a clerk at Pickford & Co that (i) the mill had stopped and that the crank shaft needed to be sent immediately, and (ii) if a special entry was necessary to hasten the delivery, then such an entry should be made.<sup>35</sup> The clerk at Pickford & Co said that the crank shaft would be delivered to the engineers "on the second day after the day of ... delivery" to Pickford & Co.<sup>36</sup> Pickford & Co failed to deliver the crank shaft in this time. They chose to send the crank shaft by water several days later rather than sending it

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<sup>26</sup> *Black v Baxendale* (1847) 1 Ex 410 at 410, 154 ER 174 (Exch) at 174–175.

<sup>27</sup> At 410–411. See also Danzig, above n 23, at 256.

<sup>28</sup> *Black v Baxendale*, above n 26, at 411.

<sup>29</sup> At 411–412. See further F Faust "Hadley v. Baxendale – an Understandable Miscarriage of Justice" (1994) 15 JLH 41 at 43–44.

<sup>30</sup> *Black v Baxendale*, above n 26, at 411–412.

<sup>31</sup> *Waters v Towers* (1853) 8 Ex 401, 155 ER 1404 (Exch).

<sup>32</sup> Kent, above n 20, at 665.

<sup>33</sup> *Hadley v Baxendale*, above n 5, at 341.

<sup>34</sup> At 341–342.

<sup>35</sup> At 344.

<sup>36</sup> At 342.

immediately by wagon.<sup>37</sup> Consequently, it took them seven days to deliver the crank shaft to the engineers.<sup>38</sup>

The plaintiffs sued Mr Joseph Baxendale as the London-based managing director of Pickford & Co and others. They sought £300 in damages.<sup>39</sup> The Hadleys initially brought their claim in a form which would probably be understood today as being for both breach of contract and for a tort of breach of a common carrier's duty to deliver within a reasonable time.<sup>40</sup> As to the claim for breach of contract, the defendants entered a plea of non assumpserunt.<sup>41</sup> The plaintiffs subsequently entered a nolle prosequi to the claim,<sup>42</sup> probably due to the Hadleys' uncertainty as to whether the Pickford & Co employee who accepted the crank shaft had authority to contract for delivery at the time.<sup>43</sup> So the claim was not one for breach of contract.

As to the claim based upon the common carrier's duty, Pickford & Co and Mr Baxendale paid £25 into Court and submitted that this was sufficient damages.<sup>44</sup> The Hadleys submitted that this amount was inadequate. They said that they had lost profits as a result of the unreasonable delay in delivering the crank shaft. They said they were prevented from cleaning, grinding and dressing the cornmeal, and were deprived of the opportunity to sell flour and accrue profits during that time. They said that they were obliged to buy flour to supply some of their customers. And they said that they had to pay wages to their workmen despite being unable to employ them.<sup>45</sup>

At first instance Sir Roger Crompton, the new judge on assize, left the matter to the jury, instructing them that they should consider what was a reasonable time for delivery and what damages were caused by the delay. He told the jury that they should give damages for the natural consequences of the defendants' breach of contract, so that they needed to consider whether the stoppage of the plaintiffs' work was a natural consequence of the breach.<sup>46</sup> The jury held that the defendants were liable to pay £50 in damages.<sup>47</sup>

Mr Baxendale and Pickford & Co applied to the Court of Exchequer to quash the decision and order a new trial. They submitted that the jury was misdirected because the jury members ought to have been told that the damages were too remote. In contrast, the Hadleys submitted that there was "ample evidence" that the defendants knew why the shaft was being delivered,

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<sup>37</sup> "Hadley and Another v. Baxendale and Others" *Times* (London, 8 August 1853) at 10: "It was proved that the shaft might have arrived in London and been delivered at Greenwich in the course of Monday, the 16th of May; but, instead of being forwarded by wagon immediately, it was kept for several days in London, and was at length forwarded by water on the 20th, along with many tons of iron goods which had been consigned to the same parties."

<sup>38</sup> *Hadley v Baxendale*, above n 5, at 342.

<sup>39</sup> At 343.

<sup>40</sup> See Faust, above n 29, at 48 for an analysis of the words used in Hadleys' submissions.

<sup>41</sup> *Hadley v Baxendale*, above n 5, at 343.

<sup>42</sup> At 343.

<sup>43</sup> The *Gloucester Journal* wrote shortly after the case was decided, "The declaration had originally contained two counts; the first charging the defendants with having contracted to deliver the crank within the space of two days, which they did in truth do, but there was a doubt how far Mr. Perrett, the agent of the defendants, had authority to bind them by any special contract which would vary their ordinary liability. It was therefore thought not prudent to proceed upon that count, but upon the count of not delivering within a reasonable time":

*Gloucester Journal* (Gloucester, 13 August 1853) at 1, col 4.

<sup>44</sup> *Hadley v Baxendale*, above n 5, at 343.

<sup>45</sup> At 343.

<sup>46</sup> *Gloucester Journal*, above n 43, at 1, col 4, n 7.

<sup>47</sup> *Hadley v Baxendale*, above n 5, at 345.

and that a failure to deliver it within time would result in a stoppage of the mill.<sup>48</sup> The Hadleys' counsel referred to a series of English cases – “indiscriminately in contract and in tort”<sup>49</sup> – as evidence of the law’s recognition of loss of profits, even though the Hadleys’ claim was based on the fact that the defendant was a common carrier (and not for breach of contract).<sup>50</sup>

### ***The decision in Hadley v Baxendale***

In *Wilson v Newport Dock Co*, Pollock CB observed that judgment in *Hadley v Baxendale* was remarkably reserved for several weeks.<sup>51</sup> In an era where few judgments were reserved, the remarks of Pollock CB were intended to emphasise how seriously the case had been taken, and the “great pains [that] were bestowed upon it”.<sup>52</sup> Pollock CB continued, adding that a number of factors “never combined to assist at the formulation of any decision”.<sup>53</sup> Those factors were Lord Wensleydale’s (Parke B) and Alderson B’s “extensive and accurate knowledge of decisions in our law books, and ... acute power of analyzing and discussing them” and, in a backhanded compliment to Martin B (who also sat in *Wilson*), Martin B’s “acquaintance with the exigencies of commerce and the business of life”.<sup>54</sup> Curiously, although Martin B agreed in the result in *Hadley v Baxendale*, he later refused to apply it to cases of ‘direct’ loss.<sup>55</sup> He also sought to confine the reasoning of *Hadley v Baxendale* in later cases and expressed agreement with Crompton J’s later approach which had sought to ring-fence *Hadley v Baxendale*.<sup>56</sup>

The Court of Exchequer, led by Alderson B (Parke and Martin BB agreeing), held in *Hadley v Baxendale* that the jury had been misdirected, and ordered a new trial.<sup>57</sup> The Court set out the rule that the judge, at the next trial, should communicate to the jury. That rule is as

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<sup>48</sup> At 349.

<sup>49</sup> D Ibbetson *A Historical Introduction to the Law of Obligations* (Oxford University Press, Oxford, 1999) at 231.

<sup>50</sup> *Hadley v Baxendale*, above n 5, at 346–349.

<sup>51</sup> *Wilson v The Newport Dock Co*, above n 6, at 189.

<sup>52</sup> At 189.

<sup>53</sup> At 189.

<sup>54</sup> At 189.

<sup>55</sup> *Collard v The South Eastern Railway Company* (1861) 7 H & N 79 at 86, 158 ER 400 (Exch) at 403: “It seems to me that *Hadley v. Baxendale* ... has no bearing on this case ... In my judgment the plaintiff is entitled to recover for this damage, because it is a direct and immediate loss consequent on the defendants’ breach of duty”. Similarly, in *Wilson v The Newport Dock Company*, above n 6, at 184–185 (footnotes omitted), Martin B said that *Hadley v Baxendale* is “an authority that in a similar case such loss of profit cannot be made an element of damages, and must be excluded; but it is an authority no farther ... The decision in *Hadley v. Baxendale* is, therefore, no authority whatever in the present case, for no loss of profits is claimed, nor is it an authority that loss of profits is not a legitimate element of damages in many other cases ... I do not adopt the qualifications mentioned by Mr. Baron Alderson in the judgment in *Hadley v. Baxendale* as applicable to every case.”

<sup>56</sup> In *Wilson v The Newport Dock Company*, above n 6, at 185 (footnotes omitted), Martin B said: “As to *Hadley v. Baxendale*, I was a party to it, and have no desire to depreciate it, but in *Boyd v Fitt*, the Court of Exchequer in Ireland dissented from it, and approved of the views of the late Mr. Justice Crompton [*Smeed v. Foord*] and Sir James Wilde [*Gee v. Lancashire & Yorkshire Railway Company*], as being the sounder expositions of the law as to remoteness of damages.” In *Collard v The South Eastern Railway Company*, above n 55, at 86, Martin B said, “I think that *Smeed v Foord* was correctly decided”. In *Smeed v Foord* (1859) 1 El & El 602 at 616, 120 ER 1035 (KB) at 1040 Crompton J referred to *Hadley v Baxendale* and said, in relation to the second branch of the rule, “I doubt whether, in these cases, it is the duty of a Judge to lay down more to the jury than that the plaintiff is entitled to such damages as are the natural consequence of the breach of contract. The question, what are such natural consequences is, I think, in each case, rather for the jury than for the Judge; just as it is for them, not for him, to assess the amount of damages.”

<sup>57</sup> *Hadley v Baxendale*, above n 5, at 356.

follows, with identification in parentheses of what became known much later as the first and second limbs:<sup>58</sup>

Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it [*the first limb*]. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated [*the second limb*]. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them.

The Court held that the consequences of the crank shaft being delivered after the period of time promised was not properly communicated to the defendants.<sup>59</sup> Alderson B said that it could have been possible, for example, that the plaintiffs had another shaft in their possession which would allow them to continue work.<sup>60</sup> Alderson B also said it may have also been possible that other parts of the steam engine were also defective, and the mill would not have resumed operation after the shaft's repair.<sup>61</sup> It followed that the loss of profits was not considered to be fairly and reasonably contemplated by both parties when they made the contract.<sup>62</sup> The Court held that the loss did not flow naturally from the breach of the contract, nor were there special circumstances which were communicated to the defendants. Therefore, the jury should have been told not to take the loss of profits into consideration.

There are two question marks about the correctness of the result. First, it is curious that the decision concerning communication made no mention of the fact that the plaintiffs' employee had told a clerk at Pickford & Co that the mill had stopped and that the crank shaft needed to be sent immediately, and that a special entry to hasten the delivery should be made if necessary. There is some dispute as to whether this fact was before the superior court on appeal,<sup>63</sup> but it does appear in the headnote of the report,<sup>64</sup> and Martin B (who had concurred) later described it as one of the facts of the case.<sup>65</sup> It had not been argued at trial, and was not argued before the Court of Exchequer, that the clerk had insufficient authority to impute his knowledge to the defendants.<sup>66</sup> One explanation (based on the report of the decision in 18 Jur

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<sup>58</sup> At 354–355.

<sup>59</sup> At 355–356.

<sup>60</sup> At 355–356.

<sup>61</sup> At 356.

<sup>62</sup> At 356.

<sup>63</sup> Faust, above n 29, at 45.

<sup>64</sup> *Hadley v Baxendale*, above n 5, at 341.

<sup>65</sup> *Wilson v The Newport Dock Company*, above n 6, at 183–184.

<sup>66</sup> Compare D Pugsley “The Facts of *Hadley v Baxendale*” [1976] NLJ 420 who seeks to draw a distinction between the *times* when the clerk was told that the mill had stopped (13 May) and that a special entry should be made if needed (14 May). This appears to be a forensic point which was not argued either at trial or before the Court of Exchequer.



358) is that the defendants knew that the mill had stopped but that they did not know that it would *remain* idle.<sup>67</sup> But there is also no sign that this point had been argued.

Secondly, although the claim in *Hadley v Baxendale* was not ultimately brought for breach of contract and although Baxendale was a common carrier, the parties and the Court in *Hadley v Baxendale* seem to have assumed that the Carriers Act 1830 (UK)<sup>68</sup> did not apply. That Act provided that persons who shipped small packages of great value were required to give notice of that value to the shipper. Otherwise, their right of recovery would be limited to £10. Section 6 of the Act was ambiguous, and open to the interpretation that carriers could limit their liability for loss or injury to £10 by notice. In 1852, the Court of Exchequer in *Carr v Lancashire and Yorkshire Railway* upheld the lawfulness of exemption clauses inserted into contracts by railway companies which limited liability to £10.<sup>69</sup> This caused tension with the executive, and a bill reversing the decision was introduced into the Parliament shortly before *Hadley v Baxendale* was decided. It is possible that, as Danzig suggests,<sup>70</sup> the bench may not have raised the point with the parties at a time when Parliament was about to legislate to abolish the practice of excluding liability. There may also have been some sympathy for the defendants: Parke B (who sat on the Court) had a brother who was Baxendale's predecessor as manager of Pickford & Co; Martin B, who also sat, had previously acted as counsel for the company.<sup>71</sup>

### ***The two theories of Hadley v Baxendale***

Although, four years after *Hadley v Baxendale* was decided, a New York court relied upon the decision,<sup>72</sup> it was not initially considered as a rule of any great importance. In Anson's *Principles of the Law of Contract*,<sup>73</sup> the rule in *Hadley v Baxendale* was simply added as an addendum to the passage about *Robinson v Harman*.<sup>74</sup> Anson explained that the decision in *Robinson v Harman* stood for the proposition:<sup>75</sup>

... that where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.

*Hadley v Baxendale* was cited as one of a series of limitations to the rule in *Robinson v Harman*, but it was given only a paragraph of discussion.<sup>76</sup> Addison, too, in his 1875 text *Addison on Contracts*, dedicated little more than passing references to *Hadley v Baxendale*.<sup>77</sup> In his 1876, 1881 and 1906 editions of *Principles of Contract at Law and in Equity*, Frederick

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<sup>67</sup> As Simpson noted, this was the explanation given by Treitel in the third edition of his book: see AWB Simpson "Innovation in Nineteenth Century Contract Law" (1975) 91 LQR 247 at 276, n 30, citing GH Treitel *The Law of Contract* (3rd ed, Stevens & Sons, London, 1970) at 802, n 85.

<sup>68</sup> Carriers Act 1830 (UK) 11 Geo IV & 1 Will IV c 68, s 6.

<sup>69</sup> *Carr v Lancashire and Yorkshire Railway* (1853) 7 Ex 706, 155 ER 1133 (Exch).

<sup>70</sup> Danzig, above n 23, at 266.

<sup>71</sup> At 267.

<sup>72</sup> *Griffin v Colver* 16 NY 489 (1858).

<sup>73</sup> WR Anson *Principles of the Law of Contract* (Callaghan and Company, Chicago, 1880).

<sup>74</sup> *Robinson v Harman*, above n 21.

<sup>75</sup> Anson, above n 73, at 314–315.

<sup>76</sup> At 315–316. Similarly, *Hadley v Baxendale* was glossed over in Anson's first (1906) American edition of *Principles of the English Law of Contract*, being referred to in nothing more than a footnote: WR Anson *Principles of the English Law of Contract and of Agency in Its Relation to Contract* (11th ed, Clarendon Press, Oxford, 1906; Henry Frowde, London and New York, 1906) at 334.

<sup>77</sup> CG Addison *Addison on Contracts being a Treatise on the Law of Contracts* (7th ed, Stevens, Sons, & Warwick, London, 1875) at 362 and 779.

Pollock made no reference to *Hadley v Baxendale*,<sup>78</sup> although his texts contained little discussion about the principle of assessment of damages generally. And Joseph Chitty also included only a few references to *Hadley v Baxendale* in his 1874 edition of *A Treatise on the Law of Contracts and upon the Defences to Actions Thereon*.<sup>79</sup>

Within three decades, however, the decision became well known. John Lawson described *Hadley v Baxendale* as being “justly regarded as the leading case on the subject of damages arising from a breach of contract”.<sup>80</sup> Similar remarks were made by FE Smith.<sup>81</sup> Lord Esher MR said of the rule in *Hadley v Baxendale* that:<sup>82</sup>

It may be that the rule so laid down was not necessary for the purpose of deciding that case, but it is far too late to question it. The rule, though frequently commented upon, has been over and over again adopted by the Courts, and must now be considered to be the law on the subject.

As the rule in *Hadley v Baxendale* became well known, academic writers turned to consider the foundation for the rule. One rationale emerged that the rule reflected an objective assumption of responsibility. This rationale objectified the subjective approach from Pothier’s treatise where Pothier had written of the reasonable contemplation rule as the loss that the “debtor has expressly or tacitly submitted to”.<sup>83</sup> In Chitty’s 1874 edition of *A Treatise on the Law of Contracts and upon the Defences to Actions Thereon*, the rationale became objective. Chitty wrote:<sup>84</sup>

In an action against a carrier for the non-delivery of goods, the ordinary measure of damages is, the value of the goods to the owner, at the *place* and *time* at which they ought to have been delivered. And the owner is not entitled to recover special damages against the carrier, unless he show that, at the time the goods were delivered to be carried, the circumstances out of which such damages arose were specially made known to the carrier, in such a way as to lead to the conclusion, that he then accepted the goods with the condition attached, viz. that, in the event of a breach, he should be liable for such special damages.

Again, in the second edition of his *Treatise on the Law of Damages* published in 1872, Mayne referred to an assumption of responsibility based on *conduct* by the defendant.<sup>85</sup>

But it may be asked with great deference, whether the mere fact of such consequences being communicated to the other party will be sufficient, without going on to show that he was told that he would be held answerable for them, and consented to undertake such a liability? ... No doubt it may be said that it was in the power of the defendant to have expressly refused such responsibility. True. But ought not the onus of making a contract rather to lie on the party who seeks to extend the liability of another, than upon him who merely seeks to restrain his own within its original limits?

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<sup>78</sup> F Pollock *Principles of Contract at Law and in Equity* (Stevens and Sons, London, 1876); F Pollock *Principles of Contract at Law and in Equity* (1st American ed from 2nd English ed, Robert Clarke & Co, Cincinnati, 1881); F Pollock *Principles of Contract at Law and in Equity* (3rd American ed from 7th English ed, Baker, Voorhis & Company, New York, 1906).

<sup>79</sup> J Chitty *A Treatise on the Law of Contracts and upon the Defences to Actions Thereon* (11th American ed, Hurd and Houghton, New York, 1874) vol 1.

<sup>80</sup> JD Lawson *Leading Cases Simplified: A Collection of the Leading Cases of the Common Law* (FH Thomas & Company, St Louis, 1882) at 126.

<sup>81</sup> Smith, above n 8, at 275.

<sup>82</sup> *Hammond & Co v Bussey* (1887) 20 QBD 79 (CA) at 88.

<sup>83</sup> Pothier, above n 16, at part 1, ch 2, art 3, [165] (translated ed).

<sup>84</sup> Chitty, above n 79, at 725 (footnotes omitted).

<sup>85</sup> JD Mayne *A Treatise on the Law of Damages* (2nd ed, Stevens and Haynes, London, 1872) at 10 (footnote omitted).

In 1899, Mayne then reformulated the second limb of the rule in *Hadley v Baxendale* as follows:<sup>86</sup>

In the present state of the authorities, therefore, I would suggest that in place of the third rule supposed to be laid down by *Hadley v. Baxendale*, the law may perhaps be as follows:—

First.—Where there are special circumstances connected with a contract, which may cause special damage to follow if it is broken, mere notice of such special circumstances given to one party will not render him liable for the special damage, unless it can be inferred from the whole transaction that he consented to become liable for such special damage.

Secondly.—Where a person who has knowledge or notice of such special circumstances might refuse to enter into the contract at all, or might demand a higher remuneration for entering into it, the fact that he accepts the contract without requiring any higher rate will be evidence, though not conclusive evidence, from which it may be inferred that he has accepted the additional risk in case of breach.

Thirdly.—Where the defendant has no option of refusing the contract, and is not at liberty to require a higher rate of remuneration, the fact that he proceeded in the contract after knowledge or notice of such special circumstances is not a fact from which an undertaking to incur a liability for special damage can be inferred.

Oliver Wendell Holmes also took a similar approach focusing on the objective assumption of responsibility when he said:<sup>87</sup>

If a breach of contract were regarded in the same light as a tort, it would seem that if, in the course of performance of the contract the promisor should be notified of any particular consequence which would result from its not being performed, he should be held liable for that consequence in the event of non-performance. Such a suggestion has been made. But it has not been accepted as the law. On the contrary, according to the opinion of a very able judge, which seems to be generally followed, notice, even at the time of making the contract, of special circumstances out of which special damages would arise in case of breach, is not sufficient unless the assumption of that risk is to be taken as having fairly entered into the contract. If a carrier should undertake to carry the machinery of a saw-mill from Liverpool to Vancouver's Island, and should fail to do so, he probably would not be held liable for the rate of hire of such machinery during the necessary delay, although he might know that it could not be replaced without sending to England, unless he was fairly understood to accept "the contract with the special condition attached to it."

This rationale based on assumption of responsibility was disputed. A competing theory was that the rationale for the rule in *Hadley v Baxendale* was not based upon an objective assumption of responsibility by the parties but was generally concerned with subjective knowledge of the defendant, by direct proof or by inference, because this was a policy choice about how to limit the extent to which otherwise unlimited damages were recoverable. This approach, which might be called the 'policy theory', treated subjective knowledge as a policy limit on compensation. It was the basis for the criticism of Mayne's view by FE Smith who said that it seemed to ignore completely the rationale of the rule that everyone who breaches a contract shall pay for its natural consequences.<sup>88</sup> Smith said that Mayne's view erroneously assumed "a constant uniformity in the naturalness of consequence".<sup>89</sup> He continued:<sup>90</sup>

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<sup>86</sup> JD Mayne *Mayne's Treatise on Damages* (6th ed, Stevens and Haynes, London, 1899) at 41.

<sup>87</sup> OW Holmes Jr *The Common Law* (Macmillan & Co, London, 1882) at 301–302 (footnotes omitted). Holmes' reference to the decision of a "very able judge" was a reference to Willes J's decision in *The British Columbia and Vancouver's Island Spar, Lumber, and Saw-Mill Co, Ltd, v Nettleship* (1868) LR 3 CP 499 (Comm Pleas) at 509.

<sup>88</sup> Smith, above n 8, at 280.

<sup>89</sup> At 280.

With great respect for the high authority of Mr. Mayne's work, I believe the following propositions to represent the law more accurately.

(1) The measure of damages for breach of contract is determined by the knowledge, actual or constructive, which the parties had of the probable consequences of the breach. If they contemplated, or ought to have contemplated, the consequences which have proximately followed, they are liable to pay damages accordingly.

(2) In determining what consequences the parties may be reasonably supposed to have contemplated the knowledge of the circumstances under which the contract was made must be, not merely an important, but the decisive consideration.

(3) Notice of these circumstances enlarges the area of contemplation, and therefore the liability of the defendant in an action for breach of contract.

The differences between these two approaches could have serious consequences. But the underlying theory was rarely confronted by the judiciary. Two exceptions, in 1867 and 1873, were Willes J and Kelly CB, both of whom saw the rule as one based upon assumption of responsibility rather than the policy theory based upon knowledge. As for Willes J, he had been Baxendale's counsel. As Danzig notes, Willes "was reputed to be the ablest commercial lawyer of his time"<sup>91</sup> and was described by Scrutton (according to Sir Frank MacKinnon) as "the best commercial lawyer since Lord Mansfield".<sup>92</sup> He was said to speak seven languages. Indeed, his fluency in Spanish was so great that he successfully defended himself in Spain of a charge of murder when a coachman fell under the horses of his carriage.<sup>93</sup> After elevation to the bench, Willes J explained the rationale for the basis of the rule in *The British Columbia and Vancouver's Island Spar, Lumber, and Saw-Mill Co, Ltd, v Nettleship*.<sup>94</sup>

... one of two contracting parties ought not to be allowed to obtain an advantage which he has not paid for. ... [I]t could not be contended that the mere fact of knowledge, without more, would be a reason for imposing upon him a greater degree of liability than would otherwise have been cast upon him. ... [T]he mere fact of knowledge cannot increase the liability. The knowledge must be brought home to the party sought to be charged, under such circumstances that he must know that the person he contracts with reasonably believes that he accepts the contract with the special condition attached to it.

The second judge to engage with the rationale for *Hadley v Baxendale* was Kelly CB in *Horne v Midland Railway Co*.<sup>95</sup> In that case, the question was whether railway companies, who were at that time obliged to receive and deliver goods, could be subject to unlimited liability if they had notice of extraneous circumstances. Two judges held that the company was not required to accept the goods<sup>96</sup> but the third, Kelly CB, thought that it was but that notice alone could not establish liability. He said:<sup>97</sup>

A question of very great importance has been raised in the course of the argument ... [T]he question what the position of a railway company is when goods are entrusted to it for carriage with an intimation of the consequences of non-delivery, such as it was argued on behalf of the plaintiffs existed in the present case. ... Now, it is clear, in the first place, that a railway company, such, as Mr. Field contended, this amounted to, not merely that if the goods are not

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<sup>90</sup> At 286–287.

<sup>91</sup> Danzig, above n 23, at 257.

<sup>92</sup> FD MacKinnon "Sir James Shaw Willes" (1944) 60 LT Rev at 129 as cited in Danzig, above n 23, at 257–258, n 38.

<sup>93</sup> Danzig, above n 23, at 258.

<sup>94</sup> *The British Columbia and Vancouver's Island Spar, Lumber, and Saw-Mill Co, Ltd, v Nettleship*, above n 87, at 508–509.

<sup>95</sup> *Horne v Midland Railway Co* (1873) LR 8 CP 131 (Exch Ch).

<sup>96</sup> At 145 per Lush J and 143 per Pigott B.

<sup>97</sup> At 136–137.

delivered by a certain date they will be thrown on the consignor's hands, but in express terms stating that they have entered into such and such a contract and will lose so many pounds if they cannot fulfil it, what is then the position of the company? Are they the less bound to receive the goods? I apprehend not. If, then, they are bound to receive, and do so without more, what is the effect of the notice? Can it be to impose upon them a liability to damages of any amount, however large, in respect of goods which they have no option but to receive? I cannot find any authority for the proposition that the notice without more could have any such effect. It does not appear to me that the railway company has any power, such as was suggested, to decline to receive the goods after such a notice, unless an extraordinary rate of carriage be paid.

### ***The adoption of the policy theory of Hadley v Baxendale***

A century and a half after *Hadley v Baxendale*, similar questions were put before the House of Lords for consideration in *Jackson v Royal Bank of Scotland plc*.<sup>98</sup> In that case, the claimant importer brought an action against a bank for damages for loss of profit. The claimants imported dog chews from a company in Thailand, and onsold them to a third party at significantly higher marked up prices. By accident, the bank which handled the paperwork for the payments sent to the third party documents which should have been sent to the claimants. Those documents revealed the marked up prices. The third party terminated the relationship it had with the claimants. The claimants sued the bank for breach of contract claiming damages for the lost opportunity to profit from the trading relationship with the third party. All of the House of Lords seemed to view *Hadley v Baxendale* as establishing a policy rule based upon knowledge of the parties, subject to any limit to the liability that the parties recognised in their contract. However, damages were limited to four years' worth of lost profits on a reducing basis, because anything beyond four years was considered to be too speculative.<sup>99</sup> Lord Walker of Gestingthorpe stated:

The common ground of the two limbs [of *Hadley v Baxendale*] is what the contract-breaker knew or must be taken to have known, so as to bring the loss within the reasonable contemplation of the parties ...

He cited Lord Reid's remarks that:<sup>100</sup>

I do not think that it was intended that there were to be two rules or that two different standards or tests were to be applied [in *Hadley v Baxendale*]. ...

...

... The crucial question is whether, on the information available to the defendant when the contract was made, he should, or the reasonable man in his position would, have realised that such loss was sufficiently likely to result from the breach of contract to make it proper to hold that the loss flowed naturally from the breach or that loss of that kind should have been within his contemplation.

Lord Hope also thought that absent any limitation in the contract:<sup>101</sup>

... there is no arbitrary limit that can be set to the amount of damages once the test of remoteness according to one or other of the rules in *Hadley v Baxendale* has been satisfied.

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<sup>98</sup> *Jackson v Royal Bank of Scotland plc* [2005] UKHL 3, [2005] 1 WLR 377.

<sup>99</sup> At [37] and [43] per Lord Hope (Lords Nicholls, Hoffman, Walker and Brown agreeing).

<sup>100</sup> *C Czarnikow Ltd v Koufos* [1969] 1 AC 350 (HL) [*The Heron II*] at 385 as cited in *Jackson v Royal Bank of Scotland plc*, above n 98, at [47].

<sup>101</sup> *Jackson v Royal Bank of Scotland plc*, above n 98, at [36].

At the time of *Jackson* other authority had already suggested that *Hadley v Baxendale* involved a single rule concerned with express or inferred knowledge.<sup>102</sup> In Australia too, in *Baltic Shipping Co v Dillon* Brennan J said the rules in *Hadley v Baxendale* had been merged into a single principle,<sup>103</sup> citing *C Czarnikow Ltd v Koufos*,<sup>104</sup> *Wenham v Ella*,<sup>105</sup> *Burns v MAN Automotive (Aust) Pty Ltd*,<sup>106</sup> and *Commonwealth v Amann Pty Ltd*.<sup>107</sup> And the High Court of Australia in *European Bank Ltd v Evans* confirmed that the two limbs of the rule in *Hadley v Baxendale* are properly understood as representing a single principle which “may depend on the degree of relevant knowledge possessed by the defendant in the particular case”.<sup>108</sup>

### ***Two difficulties with the policy theory of Hadley v Baxendale***

The theoretical basis for the policy theory of *Hadley v Baxendale* is beguilingly simple. It involves two propositions. The first proposition is that damages in both limbs of *Hadley v Baxendale* are concerned with compensation for loss. As a matter of corrective justice, a wrongdoer who breaches the rights of another should rectify the consequences as far as money can do it. In *Parry v Cleaver*,<sup>109</sup> Lord Reid explained that *British Transport Commission v Gourley*<sup>110</sup> had made clear that it is a universal rule that a plaintiff cannot recover more than he or she has lost. This universal principle was reiterated in the High Court of Australia in *Haines v Bendall*,<sup>111</sup> where Mason CJ, Dawson, Toohey and Gaudron JJ said that compensation for loss suffered is the “one principle that is absolutely firm, and which must control all else”.<sup>112</sup> The principle sounds obviously correct. If courts are to compensate for loss then they should not provide more compensation than loss.

The second proposition is that a wrongdoer should not, as a matter of policy, be responsible for every consequence of wrongdoing ad infinitum. As Washington put it in 1932, a contracting party could not be an “absolute insurer” and a “workable division of the risks must be effected, and it is a compromise of this kind which is achieved by the operation of the principle of reasonableness and foresight”.<sup>113</sup> Rules of remoteness are therefore necessary to ensure proportionality between the wrongdoing and the responsibility for its consequences. *Hadley v Baxendale* provides that rule of policy. As Roth J more recently explained, “The concept of remoteness is a limiting principle on the damages that may be recovered based on considerations of policy.”<sup>114</sup>

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<sup>102</sup> See *Smeed v Foord*, above n 56, at 616 per Crompton J; *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528 (CA) at 539 per Asquith LJ; *Kpohraror v Woolwich Building Society* [1996] 4 All ER 119 (CA) at 127–128 per Evans LJ; *H Parsons (Livestock) Ltd v Uttley Ingham & Co Ltd* [1978] QB 791 (CA) at 813 per Scarman LJ; *C Czarnikow Ltd v Koufos*, above n 100, at 385 per Lord Reid.

<sup>103</sup> *Baltic Shipping Co v Dillon* [1993] HCA 4, (1993) 176 CLR 344 at 368, n 20.

<sup>104</sup> *C Czarnikow Ltd v Koufos*, above n 100, at 385 per Lord Reid.

<sup>105</sup> *Wenham v Ella* [1972] HCA 43, (1972) 127 CLR 454 at 471.

<sup>106</sup> *Burns v MAN Automotive (Aust) Pty Ltd* [1986] HCA 81, (1986) 161 CLR 653 at 667.

<sup>107</sup> *Commonwealth v Amann Pty Ltd* [1991] HCA 54, (1991) 174 CLR 64 at 92 per Mason CJ and Dawson J and 99 per Brennan J.

<sup>108</sup> *European Bank Ltd v Evans* [2010] HCA 6, (2010) 240 CLR 432 at [13] per French CJ, Gummow, Hayne, Heydon and Kiefel JJ.

<sup>109</sup> *Parry v Cleaver* [1969] UKHL 2, [1970] AC 1 at 13.

<sup>110</sup> *British Transport Commission v Gourley* [1956] AC 185 (HL).

<sup>111</sup> *Haines v Bendall* [1991] HCA 15, (1991) 172 CLR 60 at 63.

<sup>112</sup> *Skelton v Collins* [1966] HCA 14, (1966) 115 CLR 94 at 128 per Windeyer J as cited in *Haines v Bendall*, above n 111, at 63.

<sup>113</sup> Washington, above n 22, at 107.

<sup>114</sup> *Wellesley Partners LLP v Withers LLP* [2015] EWCA Civ 1146, [2016] Ch 529 at [145].

*Difficulties with the first proposition of a concern only with compensation for loss*

The first proposition has been disputed. The argument made by those who dispute it is that the first limb of *Hadley v Baxendale*, and the concern with damages “according to the usual course of things”<sup>115</sup> embodies a fundamentally different concern from the second limb which is concerned with limits to compensation based upon the defendant's knowledge. The argument, most recently made by Dr Winterton, is that the first limb is not concerned with compensation for loss at all. Instead, it is argued that the first limb is a form of monetised specific performance.<sup>116</sup> On this view, damages should be calculated as the reasonable cost of obtaining substitute performance or the reasonable price for granting a release from obligations. In each case, the money payment provides a substitute for the performance that should have been undertaken. In that sense, these damages have more in common with enforcement of a primary right, such as a claim for payment of a debt. It therefore makes sense that these damages cannot increase or decrease by subsequent events. Such ‘normal damages’ focus upon securing the entitlement promised to a claimant rather than attempting to eradicate, as far as reasonable, the consequential losses that arise from breach. If this approach is correct then these damages should generally be fixed at the date of breach.<sup>117</sup>

There are cases which provide support, in their result although rarely in their reasoning, for Dr Winterton’s view. The ‘usual’ measure of damages is awarded despite later events demonstrating that the claimant did not suffer any loss. A circumstance which illustrates this controversy is in the sale of goods.<sup>118</sup> In *Slater v Hoyle*,<sup>119</sup> a buyer purchased cloth in order to fill a sub-sale to a third party. The cloth was supplied by the seller in breach of contract because it was of inferior quality but the sub-purchaser accepted it, paid the above market price, and took no legal proceedings. Nevertheless, the Court of Appeal held that the ‘loss’ was the difference between the market value of sound goods and the market value of damaged goods. The result appears to be an award of the money value of the promised performance rather than any assessment of loss to the claimant. However, the result in *Slater v Hoyle* was rejected in *Bence Graphics International Ltd v Fasson UK Ltd*.<sup>120</sup> In that case, the defendants had supplied defective vinyl film to the claimants. The claimants sought the ‘normal’ or ‘usual’ first limb measure of the difference in value between the vinyl film supplied and the vinyl film which had been promised. The primary judge accepted this submission and awarded damages of £564,328. The defendants appealed, arguing that the parties were aware at the time of contract that the vinyl would be unsold and the claimants had unsold the vinyl without loss. Hence, as Otton LJ said:<sup>121</sup>

... at the time of making their contract the parties were aware of facts which indicated to both that the loss would not be the difference between the value of the goods delivered and the market value ...

A majority of the Court of Appeal (Otton and Auld LJJ; Thorpe LJ dissenting) held that the matter should be remitted to the trial judge for assessment of the true loss suffered. In *Bence*

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<sup>115</sup> *Hadley v Baxendale*, above n 5, at 354.

<sup>116</sup> D Winterton *Money Awards in Contract Law* (Hart Publishing, Oxford, 2015).

<sup>117</sup> With exceptions such as those recognised by Chalmers where the buyer prepays for the goods, or where the seller repudiates the contract before the time of delivery.

<sup>118</sup> As Sir Mackenzie Chalmers explained, the sale of goods legislation that he drafted was intended to be a reproduction of the common law as it was at the time: M Chalmers *The Sale of Goods Act, 1893, Including the Factors Acts, 1889 & 1890* (2nd ed, William Clowes and Sons, London, 1894) at iv. See also M Chalmers *The Sale of Goods, Including the Factors Acts, 1889* (William Clowes and Sons, London, 1890) at v.

<sup>119</sup> *Slater v Hoyle* [1920] 2 KB 11 (CA).

<sup>120</sup> *Bence Graphics International Ltd v Fasson UK Ltd* [1998] QB 87 (CA).

<sup>121</sup> At 101.

*Graphics* the majority relied upon *Hadley v Baxendale* for their conclusion. Auld LJ said that “[t]he *Hadley v. Baxendale* principle is recovery of true loss and no more (or less)”.<sup>122</sup> The *Bence Graphics* decision is not isolated. The same point had been made by Devlin J in *Biggin & Co Ltd v Permanite Ltd*,<sup>123</sup> by Lord Pearce in *C Czarnikow Ltd v Koufos*,<sup>124</sup> and by the Privy Council in *Wertheim v Chicoutimi Pulp Co*.<sup>125</sup> In the latter case, Lord Atkinson spoke of the contrary position (emphasising that it was a case of late delivery rather than non-delivery) being one which would permit the claimant.<sup>126</sup>

... against all justice, to be permitted to make a profit by the breach of contract, be compensated for a loss he never suffered, and be put, as far as money can do it, not in the same position in which he would have been if the contract had been performed, but in a much better position.

### *Difficulties with the second proposition of an imposed policy rule*

As we have seen, there was a significant debate shortly after *Hadley v Baxendale* which essentially concerned whether the decision was one which restricted damages based upon a policy rationale or based upon the limits of assumed responsibility of the parties. The dominant view which emerged was that the decision was a policy-oriented approach. But the debate has now re-emerged in England after the decision of Lord Hoffmann in *Transfield Shipping Inc v Mercator Shipping Inc (The Achilleas)*.<sup>127</sup> The *Achilleas* was a bulk carrier that was time chartered by the respondent owners to the appellant charterers. The latest date for redelivery was 2 May 2004. The owners had fixed a follow-on time charter with another company. But the charterers did not know this. When the owners realised that the vessel would not be returned in time for the follow-on charter, they had to renegotiate the charter and agree to a reduced daily rate. The total loss they suffered on the follow-on charter was USD 1,364,584. At first instance, the arbitrators held that the loss from the follow-on charter was recoverable, as it arose naturally from the breach of contract and was foreseeable. The primary judge and the Court of Appeal upheld that decision.

The charterers appealed to the House of Lords. The House of Lords allowed the appeal. They did so primarily on the basis that the volatile market conditions which caused the reduced charter rate were outside the parties’ contemplation. Lord Rodger and Baroness Hale held that the loss had not been reasonably contemplated and was too remote. As Lord Rodger explained, although some loss of business might be contemplated in the ordinary course of events, the rule in *Hadley v Baxendale* was concerned with the owners’ *particular* loss of profit which occurred in the extremely volatile market.<sup>128</sup> This conclusion might be doubted: there is a difference between abnormal losses of a different *type* and those of a different *extent*.<sup>129</sup>

In contrast with Lord Rodger and Baroness Hale, the assumption of responsibility approach was taken by Lord Hoffmann and Lord Hope. Their Lordships held that a party is liable for the express obligations assumed, but his or her liability is no greater than that for which he or

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<sup>122</sup> At 102.

<sup>123</sup> *Biggin & Co Ltd v Permanite Ltd* [1951] 1 KB 422 (KB) at 436.

<sup>124</sup> *C Czarnikow Ltd v Koufos*, above n 100, at 416.

<sup>125</sup> *Wertheim v Chicoutimi Pulp Co* [1911] AC 301 (PC) at 307–308 per Lord Atkinson.

<sup>126</sup> At 308.

<sup>127</sup> *Transfield Shipping Inc v Mercator Shipping Inc* [2008] UKHL 48, [2009] 1 AC 61 [*The Achilleas*].

<sup>128</sup> At [58].

<sup>129</sup> See *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*, above n 102.



she (objectively) assumed responsibility.<sup>130</sup> The unpredictable nature of the market was an important factor establishing that the charterer had not assumed responsibility for these losses. Additionally, according to Lord Hoffmann’s view of the evidence, there was an understanding in the shipping industry that the charterer was confined to the losses over the overrun period. Lord Hoffmann frankly acknowledged that his views were shaped by recent academic articles, which he described as “particularly illuminating”.<sup>131</sup>

Lord Walker agreed with the views of Lords Hoffmann, Hope and Rodger.<sup>132</sup> Although Baroness Hale saw a tension between the views of Lords Hoffmann and Hope (on the one hand) and Lord Rodger (on the other), it appears that Lord Walker did not see the same tension. Lord Walker’s own formulation was much closer to that of Lords Hoffmann and Hope. He described the underlying idea of ‘reasonable contemplation’ in *Hadley v Baxendale* as asking “what was the common basis on which the parties were contracting?”<sup>133</sup>

I do not attempt here to resolve this re-emerged dispute about the rationale of *Hadley v Baxendale*. It suffices to make three tentative thoughts which, when understood, might go some way to explaining why Lord Walker may have seen no tension between the two approaches. First, if *Hadley v Baxendale* were truly concerned with a policy-based limitation on responsibility for imposed damages for a breach of duty independently of the agreement of the parties, then this would invite the question of why the policy should be different from the law of torts. The answer to this question may be that the policy depends on the nature of the wrong. As the caution expressed by Crompton J in *Hadley v Baxendale* made clear, the underlying policy considerations in the law of contract generally disregard whether the defendant acted wilfully or not. Thus Crompton J had directed the jury to disregard whether the breach was wilful. In contrast, in the law of torts there is generally a different, and more liberal, remoteness test for intentional breaches. In *Quinn v Leathem* Lord Lindley said that the “intention to injure the plaintiff negatives all excuses and disposes of any question of remoteness of damage”.<sup>134</sup> However, the same ‘contractual’ approach should apply where the tort concerned is one based upon a promise. As we have seen, the decision in *Hadley* itself was concerned with the promise of a common carrier rather than a contract.<sup>135</sup> In other words, the same approach should apply to all instances of voluntary assumption of responsibility, not merely to cases where the assumption of responsibility occurs by contract. Hence, in *Wellesley Partners LLP v Withers LLP*, Longmore and Floyd LJ and Roth J all independently reached the conclusion that in cases of parallel liability in contract and in the tort of negligence based upon an assumption of responsibility, the contractual test of remoteness (as expressed in *Hadley v Baxendale*) applies.<sup>136</sup>

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<sup>130</sup> *Transfield Shipping Inc v Mercator Shipping Inc*, above n 127, at [16] per Lord Hoffmann and [31] per Lord Hope.

<sup>131</sup> At [11]. See A Kramer “An Agreement-Centred Approach to Remoteness and Contract Damages” in N Cohen and E McKendrick (eds) *Comparative Remedies for Breach of Contract* (Hart Publishing, Oxford, 2005) 249; A Tettenborn “Hadley v Baxendale Foreseeability: a Principle Beyond Its Sell-by Date?” (2007) 23 JCL 120; A Robertson “The basis of the remoteness rule in contract” (2008) 28 LS 172.

<sup>132</sup> *Transfield Shipping Inc v Mercator Shipping Inc*, above n 127, at [87].

<sup>133</sup> At [69].

<sup>134</sup> *Quinn v Leathem* [1901] AC 495 (HL) at 537. See also *Doyle v Olby* [1969] 2 QB 158 (CA) at 167 per Denning LJ; *Smith New Court Securities Ltd v Citibank NA* [1997] AC 254 (HL) at 263–265 per Lord Browne-Wilkinson (Lords Keith and Slynn agreeing) and at 281–282 per Lord Steyn (Lords Keith, Mustill and Slynn agreeing). Compare *Parabola Investments Ltd v Browallia Cal Ltd (formerly Union Cal Ltd)* [2010] EWCA Civ 486, [2011] QB 477 per Toulson LJ (Rimer and Mummery LJ agreeing).

<sup>135</sup> *Hadley v Baxendale*, above n 5, at 342.

<sup>136</sup> *Wellesley Partners LLP v Withers LLP*, above n 114, at [80] per Floyd LJ, [163] per Roth J, and [186]–[187] per Longmore LJ.

Secondly, the approach which sees remoteness of damage in contract as based upon an external rule of policy still needs to explain what that policy is and why it arises. If the policy is simply, as Washington suggested, a compromise between (i) the recovery of all losses caused by the breach and (ii) the expectations of the business community, then *why* are the expectations of the business *community* relevant to a particular contract? Surely it would be more relevant to focus on the expectations of the particular parties to the contract? And if we are to disregard their subjective expectations then the expectations could only be determined by a construction of the contract in its circumstances as it would be understood by a reasonable person. Of course, there may be nothing at all about the contract from which any assumption of responsibility can be derived. In that case, the knowledge of the parties or the usual course of things will generally be the best indicators of the extent of the liability assumed. If that is correct, then the two approaches – policy and assumption of responsibility – begin to collapse into each other. This might also explain why different cases have adopted different formulations of the degree to which a breach needs to be reasonably foreseeable. For instance, differences in formulation of the knowledge required such as “serious possibility”,<sup>137</sup> “not unlikely”,<sup>138</sup> “on the cards”,<sup>139</sup> “liable to result”<sup>140</sup> might all depend upon the nature of the assumed responsibility as the limit to damages in the circumstances of the particular contract.

Thirdly, there are grave difficulties in applying the knowledge rule in *Hadley v Baxendale* as a sufficient test for the limits of liability for contractual damages. For instance, where there is no discretion to refuse a contract then it may be that, as Kelly CB held in *Horne v Midland Railway Co*,<sup>141</sup> there cannot be an assumption of responsibility for the additional loss. Extrajudicially, an example given by Lord Hoffmann was that of a taxi cab driver, a person who is bound to accept a contract and bound to charge a fixed rate.<sup>142</sup> The example Lord Hoffmann gave is a man who tells his taxi-driver that unless he gets to his destination within a reasonable time, he will lose a £5 million deal. If the driver misreads his GPS and takes his fare to Perth instead of Glasgow, is he liable for £5 million damages? Lord Hoffmann said that it would not seem fair that even this foreseeable damage is recoverable, because he was only permitted to charge the passenger what was displayed on the meter (and not more to reflect any increase in potential liability).<sup>143</sup> In this example, the taxi-driver cannot reasonably be regarded as having accepted greater liability than that to which he would otherwise be subject.<sup>144</sup>

### ***Conclusions: back to academics and a need for theory***

*Hadley v Baxendale* was a fairly unremarkable decision. The result may have been wrong on the facts. The judges, borrowing from academic work, set out a rule which had been taken from civil law. But, unlike the academic work upon which they relied, they did not explain

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<sup>137</sup> *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*, above n 102, at 540 per Asquith LJ; *Monarch Steamship Co Ltd v Karlshamns Oljefabriker (A/B)* [1949] AC 196 (HL) at 233–234 per Lord du Parc.

<sup>138</sup> See the discussion in *C Czarnikow Ltd v Koufos*, above n 100, at 383, 388, 390 and 392 per Lord Reid, at 406 and 397 per Lord Morris, and at 414 per Lord Pearce. The Court of Appeal adopted “probable”: see *C Czarnikow Ltd v Koufos* [1966] 2 QB 695, at 732 per Diplock LJ and 722 per Sellers LJ.

<sup>139</sup> *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*, above n 102, at 540 per Asquith LJ.

<sup>140</sup> At 539–541 per Asquith LJ.

<sup>141</sup> *Horne v Midland Railway Co*, above n 95.

<sup>142</sup> L Hoffmann “The *Achilles*: Custom and Practice or Foreseeability?” (2010) 14 *Edinburgh L Rev* 47.

<sup>143</sup> At 53 and 56.

<sup>144</sup> At 56.

the rationale or basis for the rule. It fell to the leading academic lawyers of the late 19th century to attempt to explain the basis for the decision. One hundred and fifty years later the debate about the rationale for the rule has re-emerged. A prime catalyst for the re-emergence of the debate, as Lord Hoffmann acknowledged, was academic writing. Despite the fact that the power of academic thinking has been delayed for more than a century and a half in its effect of causing the law to confront its rationale, I think that the interaction in this area between academia and the judiciary is one about which Frank Guest would have been delighted.