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HADLEY V. BAXENDALE: CONTRACT DOCTRINE OR COMPENSATION RULE?

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I. HISTORY

If you do me a wrong, the ripple effects of that wrong may well—as any philosopher or insurance analyst will tell you—extend almost as far as you like. Some 180 years before the events at Hadley's Mill, commemorated in this conference, lawyers in England had to deal with the question of whether legal liability was equally susceptible to this outgrowth of chaos theory. Take a case of 1674, so briefly reported that we can reproduce it in full:

> The plaintiff declares, that the defendant in consideration of £10 promised to let him enjoy certain iron mills for six months; and it appeared that the iron mills were worth but £20 per annum, and yet damages were given to £500 by reason of the loss of stock laid in; and *per curiam* the Jury may well find such damages, for they are not bound to give only the £10 but also all the special damages.[1]

This result, obvious to us, clearly surprised at least someone then, or it would not have been reported (or for that matter appealed). But it is cases such as these—£500 damages for deprivation of a benefit worth a mere £10—that set the scene for arguments about remoteness. Unless liability for long-tail consequential losses is to be entirely open-ended, some *ad hoc* way to limit them has to be found. There are, of course, a number of possible means at hand. In the years before 1854,

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1. Nurse v. Barnes, 83 Eng. Rep. 43 (K.B. 1674). Results like this continued to attract comment surprisingly late. In the post-*Hadley* case of *Mullett v. Mason*, there is this illuminating aside from Willes, J.: "There was a case in the Exchequer tried before me at Newcastle spring assizes, 1859, in which a chemist who sold ointment to rub sheep with was held liable to pay to their owner the whole of their value, [£2,000] and upwards, it having killed them; although it was hard that a man who could only make a profit of a few pence should be made responsible for so heavy a loss." Mullett v. Mason, (1866) 1 L.R.-C.P. 559, 561.

the courts experimented with several of them (though one would be hard put to it to extract any clear results from this experimentation).[2] Thus, the courts sometimes took refuge in fairly vague doctrines such as causation (did the wrong really cause the damage?).[3] On other occasions, the courts regarded the matter as turning on the content of the duty itself.[4] Sometimes they simply relied on a more vague or impressionistic test that made it clear that some remote losses could not be claimed; however, this test was decidedly non-committal as to the precise grounds of non-liability.[5] But a test of foreseeability of some sort eventually prevailed,[6] and—as everyone knows—was finally cemented in *Hadley v. Baxendale*.[7]

Now, *Hadley v. Baxendale* is of course a breach of contract case, and is today invariably taught as part of the contracts course. For a student to mention it in, say, a torts essay is regarded by most as a serious mistake—an error demonstrated, as any law professor will confirm, by high authority on both sides of the Atlantic.[8] But at this point a conundrum arises: why should this be? Why should *Hadley v. Baxendale* be confined to contract, given that it aims to solve the problem of over-extended liability for consequential losses, and that this problem arises in tort just as much as in contract?

In looking for an answer to this problem, one thing is clear: we have to look at events substantially after 1854. Prior to *Hadley*, there was

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2. *See* A.W.B. Simpson, *Innovation in Nineteenth Century Contract Law*, 91 LAW Q. REV. 247, 273–77 (1975).

3. *See, e.g.*, Boorman v. Nash, 109 Eng. Rep. 54, 56–57 (K.B. 1829) (stating damage must have necessarily resulted); Short v. Kalloway, 113 Eng. Rep. 322 (Q.B. 1839).

4. *See* Borrodaile v. Brunton, 129 Eng. Rep. 491, 492 (C.P. 1818) (holding that the warrantee for breakage of an anchor cable extended to the possibility of loss of the anchor itself).

5. *See* Walton v. Fothergill, 173 Eng. Rep. 174, 176 (C.P. 1835) (Tindal, C.J.) ("I have a very strong opinion on the question of damages. I think they must be the necessary and immediate consequence, and not so remote as those sought to be recovered."); *see also* 2 JAMES KENT, KENT'S COMMENTARIES 480 (4th ed. 1840) ("Damages for breaches 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 and consequential losses.").

6. *See, e.g.*, Black v. Baxendale, 154 Eng. Rep. 174, 175 (Ex. 1847) (discussing breach of contract by a carrier, incidentally the same carrier as in *Hadley*); McAlpin v. Lee, 12 Conn. 129, 133 (1837) (holding no liability for "collateral loss or damage not naturally resulting from the breach of contract"); *see also* Middlekauff v. Smith, 1 Md. 329, 341–44 (1851); WILLIAM W. STORY, A TREATISE ON THE LAW OF CONTRACTS NOT UNDER SEAL § 1022 (2d ed. 1847) ("[T]he consequential injury fairly and naturally resulting to the plaintiff from the breach will be a ground for additional compensation. But merely speculative injuries founded on uncertain future contingencies, afford no ground for damages . . . .").

7. 156 Eng. Rep. 145 (Ex. 1854).

8. *See In re* Kinsman Transit Co., 338 F.2d 708, 724 (2d Cir. 1964); Koufos v. C. Czarnikow, Ltd., [1967] 3 All E.R. 686, 692 (H.L.). Both *Kinsman* and *Koufos* state fairly explicitly that *Hadley v. Baxendale* has no part to play in tort suits.

little, if any, sign that anyone regarded the doctrine of remoteness as applying differently in contract and tort. If anything, the reverse was the case: remoteness was regarded as a unitary doctrine affecting remedies as a whole. Thus, there were clear mid-nineteenth-century suggestions that tort damages were constrained by a foreseeability test fairly similar to that in *Hadley*. Take the 1850 English decision in *Rigby v. Hewitt*,[9] a completely ordinary traffic accident case, save that the events leading to the plaintiff's injury were somewhat tortuous.[10] There, Pollock CB clearly inclined to the view that tort liability extended only to "consequences that may reasonably be expected to result,"[11] an opinion he repeated elsewhere.[12] And, in case this discussion is thought too Anglocentric, views of this sort were amply paralleled in a number of early U.S. tort decisions.[13]

Now, it is true that *Hadley v. Baxendale* itself was argued purely as a contract case. It is also noteworthy that at least one of the authorities the court cited—Art. 1150 of the French Civil Code[14]—referred specifically to contractual rather than delictual liability. Nevertheless, this is probably not a fact to be taken too seriously. Even after *Hadley v. Baxendale* was decided, a respectable line of authority in England continued to reason in a similar, general way, that all consequential claims were subject to a single remoteness rule, whatever their basis. *Matthews v. Discount Corp.*[15] in 1869, for example, involved damages for trover.[16] The defendant, who held receipts for jute for a lender

9. 155 Eng. Rep. 103 (Ex. 1850).

10. *Id.* A bus being driven too fast did not hit the plaintiff directly. Instead, a wheel came off, hit another bus carrying the plaintiff and in turn caused that bus to swerve into the sidewalk, injuring him.

11. *Id.* at 104. In the event the court declined to upset a verdict for the plaintiff. *Id.*

12. *See* Greenland v. Chaplin, 155 Eng. Rep. 104, 106 (Ex. 1850) (addressing another traffic case).

13. *See, e.g.*, Anonymous, 1 Minor 52 (Ala. 1821) (allowing liability for loss of plaintiff's reputation in action for trespass by unlawful search, only because the losses "naturally result" from the trespass); Vedder v. Hildreth, 2 Wis. 427, 429 (1853) (wrongful taking of horse and harness from plaintiff while latter was traveling: no liability for further loss caused when roads subsequently became impassable, since not a loss "resulting naturally" from the taking); *cf.* Burnap v. Wight, 14 Ill. 300, 301 (1853) (holding that damages for non-prosecution of writ must be such as "naturally result from the issuing of the writ").

14. "Le débiteur n'est tenu que des dommages et intérêts qui ont été prévus ou qu'on a pu prévoir lors du contrat, lorsque ce n'est point par son dol que l'obligation n'est point exécutée." Article 1150 of the French Civil Code corresponds to Article 1996 of the current Louisiana Civil Code, "[a]n obligor in good faith is liable only for the damages that were foreseeable at the time the contract was made." LA. CIV. CODE art. 1996 (West 1987).

15. [1870] 4 L.R.-C.P. 227 (1869).

16. *Id.* (*Matthew*'s seems to be the first non-contract case in England raising *Hadley v. Baxendale*.); *see also* France v. Gaudet, (1872) 6 L.R.-Q.B. 199, 200 (1871) (stating that *Hadley* was not applicable to trover as such, but claimant cannot recover extra damages over the value of the goods without showing defendant had knowledge of the relevant circumstances, which comes to much the same thing).

who had taken them as security, wrongfully parted with them to the by-then insolvent borrower.[17] The lender successfully recovered his loss on what thereby had become an unsecured loan to a judgment-proof debtor.[18] The result is hardly surprising; however, what is interesting is that the *Matthews* decision was specifically grounded on the basis that the loss was within the *Hadley* criteria. Again, in *Sharp v. Powell*,[19] the defendant caused a nuisance by washing down a cart in a public street on a freezing day.[20] The street iced over and a passing horse broke a leg as a result.[21] Bovill CJ denied recovery on remoteness grounds.[22] Although Bovill did not cite *Hadley*, his reasoning clearly reflected the principle contained in *Hadley*.[23] Further, if a more uncompromising statement is needed, one can find it in *The Notting Hill*.[24] Following a marine collision, owners of cargo on the innocent ship suffered a loss of profit when, as a result, their cargo was delivered late on a falling market.[25] They failed on remoteness grounds to recover this from the other vessel, Brett MR saying simply that "[t]he rule with regard to remoteness of damage is precisely the same whether the damages are claimed in actions of contract or of tort, and it has been laid down many times both in *Hadley v. Baxendale* and other cases."[26] A series of similar judicial statements persisted into the early twentieth century.[27] Nor was this a peculiarly

17. *Matthews*, [1870] 4 L.R.-C.P at 228–29.

18. *Id* at. 230–33.

19. (1872) 7 L.R.-C.P. 253.

20. *Id.* at 253–54.

21. *Id.*

22. *Id.* at 258

23. *Id.* at 253–54. "No doubt, one who commits a wrongful act is responsible for the ordinary consequences which are likely to result therefrom; but, generally speaking, he is not liable for damage which is not the natural or ordinary consequence of such an act, unless it be shewn that he knows, or has reasonable means of knowing, that consequences not usually resulting from the act are, by reason of some existing cause, likely to intervene so as to occasion damage to a third person." *Id.* at 258. The parallel with Baron Alderson's formulation in *Hadley* is too close to be coincidental.

24. (1884) 9 P.D. 105 (C.A.).

25. *Id.* at 105–06.

26. *Id.* at 113 (footnote omitted). Indeed, the court then proceeded straightforwardly to follow precedent established in the earlier case of *The Parana*. *See id. The Parana* was a contract case applying *Hadley v. Baxendale* on fairly similar facts to *The Notting Hill*, the defendant there being a carrier who delayed in breach of contract. (1877) 2 P.D. 118 (C.A.). *The Parana* was overruled as to the application of *Hadley v. Baxendale*, however this fact does not affect the point in the text. *See* Koufos v. C. Czarnikow, Ltd., (1967) 3 All E.R. 686 (H.L.).

27. *See, e.g.*, H.M.S. London, [1914] P 72, 77 (1913) (Evans, President) ("It is settled law that the rule as to the remoteness of damage is the same whether the damages are claimed in actions of contract or of tort."). Lord Justice Greer in the Court of Appeal persisted in this view into the 1930s. *See* Haynes v. Harwood, [1934] All E.R. 103, 107 (C.A.); Flint v. Lovell, [1935] 1 K.B. 354, 359–60 (1934).

English phenomenon, a line of transatlantic authorities did much the same thing at the same time.[28]

How then, did the present orthodoxy—that a different, and more generous, rule of remoteness applies in tort—come to be accepted? It is true that the identification of contract and tort was never beyond question, and that occasional early authorities did accept that *Hadley* was inapplicable to tort.[29] But, the impetus for the systematic separation of tortious and contractual liability, it is suggested, arose from two factors in particular. Both arose from certain features of the then burgeoning tort of negligence. The first of these was the establishment of the rule that the defendant was liable for injuring a plaintiff—in modern terms, owed her a duty of care—if it was even remotely foreseeable that she might suffer damage as a result of his actions. The second was the "thin skull" rule, whose corollary was that the defendant was liable for the full extent of damage suffered by an unusually vulnerable plaintiff. From the 1870s, both of these were perceived to cause difficulties for courts pressed to apply *Hadley* in the tort context.

Take first the duty of care. The degree of foreseeability required to establish a duty of care has always in practice been much less than that required under *Hadley*. But, if that degree of foreseeability is established, it then hardly makes sense to take away with the left hand what has just been given by the right by saying that the loss is too remote and therefore the plaintiff cannot recover after all. An 1871 federal decision from California, rejecting the application of *Hadley v. Baxendale* in tort, demonstrated the point nicely.[30] *Bowas v. Pioneer Tow Line*, was a classic river collision case, in which a barge under tow carelessly rammed a stern-wheeler from behind.[31] As luck would

28. For representative cases applying *Hadley* criteria to tort situations see Griffith v. Burdon, 35 Iowa 138 (1872) (conversion); Balt. & Ohio R.R. Co. v. Carr, 17 A. 1052, 1054 (Md. 1889) (assault by railroad conductor); and W. Union Tel. Co. v. Short, 14 S.W. 649, 651 (Ark. 1890); and Ferrero v. W. Union Tel. Co., 9 App. D.C. 455, 464 (D.C. Cir. 1896) (negligence suits by recipients of garbled telegraphic messages, an extraordinarily prolific source of litigation in the US in the late nineteenth century). See too the seminal case of *Milwaukee & Saint Paul Ry. Co. v. Kellogg*, 94 U.S. 469, 475 (1876) (holding that run-on fire damage recoverable only if "ought to have been foreseen").

29. *E.g.*, France v. Gaudet, (1872) 6 L.R.-Q.B. 199, 200 (1871) (holding that no analogy with *Hadley* could be drawn in conversion cases); *see also* Marsh v. Joseph, [1897] 1 Ch. 213, 231 (C.A. 1896); Gibson v. Fischer, 25 N.W. 914 (Iowa 1885) (declining to apply *Hadley* to nuisance); Heister v. Loomis, 10 N.W. 60, 61 (Mich. 1881) (declining to apply *Hadley* to battery); Cate v. Cate, 50 N.H. 144, 149 (1870) (declining to apply *Hadley* to trespass).

30. 3 F. Cas. 1024, 1028 (D. Cal. 1871) (No. 1713); *see also* A.F. Johnson & Son v. Atl. Coast Line R.R. Co., 53 S.E. 362, 364 (N.C. 1906) (railroad liable for fire damage even though unforeseeable under *Hadley* test). The result in *A.F. Johnson & Son* was paralleled in an earlier England case. *See* Smith v. London & S.W. Ry. Co., (1872) 6 L.R.-C.P. 14 (Ex. Ch. 1870).

31. *Bowas*, 3 F. Cas. at 1025.

have it, an engineer was then working on (or rather in) the wheel, and was badly injured.[32] Not surprisingly, the court said the engineer could sue, even though it was hardly foreseeable within *Hadley v. Baxendale* that he would be there at the time.[33] Further the court chose to allow the action on the simple basis that a different rule applied in tort.[34]

In regard to the "thin skull" rule, the potential for mismatch was equally clear. A defendant took the vulnerable plaintiff as he found her, *even if her vulnerability was entirely unforeseeable to him.* To that extent, his liability clearly extended beyond the *Hadley* criteria to damage he could never have contemplated at all. It was an English case that seems first to have invoked this point as a reason to confine *Hadley* to contract. *Phillips v. London & South Western Railway Co.*,[35] in 1879 was an ordinary railroad negligence suit, the only complication being that the plaintiff who had been wrongfully disabled was an extraordinarily (and unforeseeably) well-paid physician.[36] The Court of Appeals had no difficulty in saying that the unforeseeable size of the income was out of account.[37] The defendants had to take the plaintiff as they found him.

Cases, such as those referred to above, started the movement. From then onwards we can trace the growth of the idea that remoteness in tort is analytically different from that in contract. In England, a unitary jurisdiction, picking up the trail is not too difficult. The case that effectively cemented the issue was *The Argentino*[38] in 1888. The point was simple (and commercially vital). Could the owners of a ship disabled in a maritime collision recover lost charter profits from the owners of the vessel in fault? In the Court of Appeals, one judge held they could not, on the basis that these earnings would not have been in the defendants' contemplation under *Hadley*'s case. But the majority held that, this being a tort suit, *Hadley* had no application, and allowed the claim.[39] After *The Argentino* was decided, a steady stream of English cases[40] accepted that the *Hadley* limitations

32. *Id.*
33. *Id.* at 1028.
34. *Id.* at 1028–29.
35. [1874–1880] All E.R. Rep. 1176 (C.A. 1879).
36. *Id.* at 1177 (indicating the plaintiff was earning something like £5,000 per annum, equivalent then to about $25,000).
37. *See id.* at 1181–80.
38. (1888) 13 P.D. 191 (C.A.). An appeal to the House of Lords was unsuccessful. *See* The Argentino, (1889) 14 App. Cas. 519 (H.L.).
39. The Argentino, (1889) 14 A.C. 519 (H.L.).
40. *E.g.*, Marsh v. Joseph, [1897] 1 Ch. 213, 231 (C.A. 1896); The Canadian Transport, 43 Lloyd's List L. Rep. 409, 410–11 (C.A. 1932) (Scrutton, L.J.); The Arpad, (1934) P. 189, 200 (C.A.) (Scrutton, L.J.). In *Addis v. Gramophone Co.*, Lord James added a practical note stating that when he was a junior at the bar, he always pleaded in tort rather than contract when possible precisely because of the more generous rules of remoteness. Addis v. Gramophone Co., [1909] A.C. 488, 492 (H.L.). More recently, an American commentator has made a similar point. *See* Banks McDowell,

did not apply in tort; a development paralleled once again in the U.S.[41]

For a time, indeed, the breach appeared absolute, because the accepted view came to be that a tort defendant's liability for consequential loss was not only outside the *Hadley v. Baxendale* remoteness rule, but was unaffected by any foreseeability criterion at all.[42] When in 1961, the English courts decided that consequential damages in tort were after all subject to a foreseeability limitation,[43] it might have been expected that this would presage a return to the application of *Hadley v. Baxendale* in tort cases as with contract ones. But doubts were expressed as to this some six years later,[44] and in 1969, Lord Reid in the House of Lords regarded it as clear that the degrees of foreseeability required were different, with a much laxer test applying in tort.[45] Equally, it is hard today to find much support in the U.S. for the application of *Hadley* in tort.[46]

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41. *See, e.g.*, W. Union Tel. Co. v. Ford, 70 S.E. 65, 68 (Ga. Ct. App. 1911) (refusing to apply *Hadley* limitations to negligent failure to deliver telegram case); W. Union Tel. Co. v. Biggerstaff, 97 N.E. 531, 533 (Ind. 1912) (refusing to apply *Hadley* limitations to tortious telegram loss); McCurdy v. Wallblom Furniture & Carpet Co., 102 N.W. 873, 875 (Minn. 1905) (declining to apply *Hadley* limitation in case of conversion); Hudson v. Atl. Coast Line R.R. Co., 55 S.E. 103, 105 (N.C. 1906) (fire damage suit against railroad for emitting sparks); A.F. Johnson & Son v. Atl. Coast Line R.R. Co., 53 S.E. 362 (N.C. 1906) (fire damage suit against railroad for emitting sparks); Garland v. Carolina, Clinchfield, & Ohio Ry., 90 S.E. 779, 779 (N.C. 1916) (declining to apply *Hadley* limitation to damages suit in tort against railroad by passenger carried beyond her stop).

42. *See In re* Polemis, [1921] 3 K.B. 560, 577 (C.A.) (stating what has become known as the "Polemis rule"); *see also* Spade v. Lynn & Boston R.R., 52 N.E. 747, 748 (Mass. 1899); Christianson v. Chi., St. Paul, Minneapolis & Omaha Ry. Co., 69 N.W. 640, 641 (Minn. 1896).

43. Overseas Tankship (U.K.) Ltd. v. Morts Dock & Eng'g Co. (The Wagon Mound), (1961) 1 A.C. 388 (H.L.) (appeal taken from Sup. Ct. of N.S.W., Austl.). Strictly speaking this was a Privy Council decision on appeal from Australia, but no one doubted then or subsequently that the decision represented English law as well.

44. Lord Reid suggested that, as regards remoteness, "[t]here has in recent times been much development of the law of torts, and developments in the law of contract may not have proceeded on parallel lines." Overseas Tankship (U.K.) Ltd. v. Miller S.S. Co. (The Wagon Mound (No. 2)), [1967] 1 A.C. 617, 638 (P.C. 1966) (appeal taken from Sup. Ct. of N.S.W., Austl.).

45. *See* Koufos v. C. Czarnikow, Ltd., (1967) 3 All E.R. 686 (H.L.) (a case well-known to students on both sides of the Atlantic for its varied exegeses of the degree of foreseeability required under *Hadley*); *see also* Henderson v. Merrett Syndicates Ltd., [1995] 2 A.C. 145, 185 (H.L. 1994) (restating this orthodoxy in a passing reference).

46. *See In re* Kinsman Transit Co., 338 F.2d 708, 724 (2d Cir. 1964) ("[T]he rule of *Hadley v. Baxendale* has no place in negligence law." (alteration in original) (citation omitted)); *see also* Vanderbeek v. Vernon Corp., 50 P.3d 866, 871 (Colo. 2002); Kuehl v. Freeman Bros. Agency, 521 N.W.2d 714, 718 (Iowa 1994).

II. SKEPTICISM

So far so good. As far as most commentators are concerned, whatever the position may have been at an earlier time, the position today is clear, and *Hadley* is confined to contract.

Or is it? Despite the prevailing orthodoxy, I must confess to some skepticism here. This is for three reasons: first, the orthodox position is more often asserted than argued for, and when one looks more closely at the arguments in support of it, it becomes increasingly clear that they do not hold up. Secondly, there are powerful arguments the other way, i.e., in favour of regarding the *Hadley* rule as a general principle of compensation law, without reference to the type of suit involved. Thirdly, it is arguable that if one looks at what courts do rather than what they say, the tendency—at least in England—has been to apply *Hadley*-style criteria to consequential claims in tort as much as in contract.

A. *Arguments for Limiting Hadley to Contract*

Although the point is not often discussed as a matter of principle, it is suggested that the arguments in favour of limiting *Hadley* to contract essentially amount to four. I will deal with each in turn.

The first two relate to points already mentioned above. Let us begin with the argument that *Hadley* cannot logically be applicable to the tort of negligence, because the degree of foreseeability of harm necessary to create that liability is admittedly a great deal lower than that required under *Hadley*. This contention probably lies at the bottom of most of the statements that the rule of remoteness is more generous in tort than contract, but, with respect, it is not very convincing. For one thing, analytically the argument can only apply at all to some torts: namely, negligence and analogous causes of action (such as nuisance, strict liability for extra-hazardous acts, etc.) in which the duty problem arises in the same way as in negligence—that is, where a foreseeable plaintiff is a prerequisite of liability.[47] To others, such as trespass or conversion, where the incidence of liability is clear and the only issue is its extent, it is simply irrelevant. More importantly, however, even if we limit our consideration to negligence and similar torts, it has to be noted that the lax foreseeability requirement there, was developed in connection with questions of the *creation* of liability[48]—that is, to the question whether the defendant owed a duty of care to the plaintiff at all. But, as we pointed out at the beginning of this

47. *See The Wagon Mound (No. 2)*, [1967] 1 A.C. at 617 (nuisance); Cambridge Water Co. v. E. Counties Leather PLC, [1994] 1 A.C. 264 (H.L. 1993) (*Rylands v. Fletcher* type liability).

48. Palsgraf v. Long Island R.R. Co., 162 N.E. 99 (N.Y. 1928); *see also The Wagon Mound*, [1961] 1 A.C. at 388; *The Wagon Mound (No. 2)*, [1967] 1 A.C. at 617. All these cases involved questions of whether the defendant was liable to this plaintiff at all, not issues of consequential loss.

paper, remoteness issues are important almost exclusively in regards to heads of consequential or "run-off" damage; the defendant's liability to pay for direct loss or damage is normally beyond question.[49] In other words, it is important here to draw a distinction between immediate and consequential loss. While it is clear *Hadley* cannot apply to a plaintiff's claim to recover in negligence for her immediate damage, this is no reason at all why it should not apply to the quantification of her recovery for consequential loss.

The second argument is the "thin skull" point. Namely, that a defendant takes the plaintiff as he finds her, without reference to the foreseeability or otherwise of her condition. This can, it is suggested, be dealt with fairly summarily. There is simply nothing inconsistent between it and a general rule requiring foreseeability of a given head of loss. It is entirely coherent to say that the plaintiff's right to recover a particular category of loss or damage depends on whether loss of that sort was foreseeable, but that once the plaintiff surmounts that hurdle, then she recovers in full for all her losses under the head concerned. Indeed, this has been held to be the case in the law of contract itself, where the "thin skull" rule, as regards a particular category of damage, coexists perfectly happily with the general applicability of *Hadley v. Baxendale* in deciding whether there can be recovery under that head in the first place.[50]

The third argument is perhaps the most formidable, at least at first sight. It runs as follows: for all their apparent similarity, when properly analysed, the issues of remoteness in contract and tort are simply not the same. In tort, remoteness rules serve an essentially social, fairness, or balancing function. In so far as we limit a tort defendant's liability for long-tail losses, we do it to avoid unfairness to him, to allow a degree of insurability, and to apply at least a degree of proportionality between wrong and loss.[51] In contract, by contrast, the matter is essentially about choice. Just as the law of contract allows a person to decide what obligations he wishes to undertake in the first place, the rule in *Hadley v. Baxendale* is at bottom about allowing him to determine what losses he will agree to cover should he break them

49. *But see* DOUGLAS LAYCOCK, MODERN AMERICAN REMEDIES 60–61 (3d ed. 2002) (arguing that basic contractual damages, such as the price-value differential, are in effect conclusively deemed foreseeable).

50. *See* Vacwell Eng'g Co. v. B.D.H. Chems. Ltd., [1971] 1 Q.B. 88 (C.A. 1969) (finding liability for catastrophic explosion even though only minor one foreseeable); H Parsons (Livestock) Ltd. v. Uttley Ingham & Co., [1978] 1 All E.R. 525, 534 (C.A. 1977) (declaring liability for death of hogs even though only slight illness foreseeable). The U.S. position very similar to the English position. *See, e.g.*, E. ALLAN FARNSWORTH, CONTRACTS § 12.14 (2d ed. 1990). For a spirited attack on the U.S. position, see Richard W. Wright, *The Grounds and Extent of Legal Responsibility*, 41 SAN DIEGO L. REV. 1425, 1480–94 (2003).

51. *E.g.*, Thomas A. Diamond & Howard Foss, *Consequential Damages for Commercial Loss: An Alternative to* Hadley v. Baxendale, 63 FORDHAM L. REV. 665, 674–77 (1994).

(or, more abstractly but perhaps more accurately, what uncertain risks associated with a possible breach he is prepared to underwrite). Hence the facts, among other things, that foreseeability is reckoned *at the time of contracting* (since this is a contractor's last chance to change his mind), and that what is required for liability under the second head is not simply knowledge of potential losses, but some indication of a common intent that the contract-breaker is content to bear responsibility for them.[52]

This is a powerful argument, especially among law and economics scholars who emphasise the peculiar facility available to contractors to adjust the incidence of potential risks by agreement among themselves.[53] Nevertheless, it is suggested that ultimately it does not hold water, for three main reasons.

To begin with, despite some early suggestions to the contrary,[54] the fact that contractual liabilities are fluid and open to adjustment by the parties does not mean that in contract a person is liable only for such losses as he has expressly or impliedly agreed to bear. On the contrary, in so far as the parties do not agree on where a given risk should lie, it now seems accepted that *Hadley v. Baxendale* is a genuine limiting device aimed at providing a default rule that will violate as few expectations as possible and provide the optimum balance between plaintiff and defendant.[55] Now, if this is right, it becomes apparent that in fact the contract remoteness rule, at least in its default form, serves much the same function as the tort one.[56] The most plausible position to adopt is one where the defendant is liable only in respect of those risks within his knowledge and control—which is effectively what *Hadley v. Baxendale* says.

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52. *See* Globe Ref. Co. v. Landa Cotton Oil Co., 190 U.S. 540, 544 (1903).

53. More precisely, the prevailing view is that *Hadley v. Baxendale* provides incentives for disclosure of information so as to allow the parties to arrive at an efficient bargain as to the losses for which each will be liable. *See, e.g.*, RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW § 4.10 (3d ed. 1986).

54. *E.g.*, *Globe Ref. Co.*, 190 U.S. at 544 (1903) (Holmes, J.) (stating that recovery "depends on what liability the defendant fairly may be supposed to have assumed consciously, or to have warranted the plaintiff reasonably to suppose that it assumed, when the contract was made").

55. English and U.S. authority now seem agreed on this principle. *See, e.g.*, FARNSWORTH, *supra* note 50, § 12.14; U.C.C. § 2-715, cmt. 2 (2004); Koufos v. C. Czarnikow, Ltd., [1967] 3 All E.R. 686 (H.L.) (Lord Upjohn); GKN Centrax Gears Ltd. v. Matbro Ltd., [1976] 2 Lloyd's Rep. 555, 574, 580 (C.A.). *But see* Kramer, *An Agreement-Centred Approach to Remoteness and Contract Damages*, *in* MCKENDRICK & COHEN, COMPARATIVE REMEDIES FOR BREACH OF CONTRACT (Hart Publishing, 2004) (arguing for the resurrection of the agreement theory).

56. *See* Thomas C. Galligan Jr., *Contortions Along the Boundary Between Contracts and Torts*, 69 TUL. L. REV. 457, 468 (1994) ("In contract law, the doctrine of consequential damages has served as a limit on the potential liability of the defendant; the same basic purpose that proximate cause has served in tort cases."). This is, of course, particularly true since the acceptance that tort damages are themselves often subject to a remoteness rule based on foreseeability.

Secondly, the distinction between imposed liability (tort) and accepted liability (contract) is less clear-cut than it seems. The standard text-book examples—on the one hand, a motorist at risk of liability who is rationally disinclined to spend resources on non-cost-effective precautions, and on the other, the seller of disembodied widgets contemplating a deal with a third party who offers more for them—are, to say the least, somewhat specialized. If one looks at, say, a professional defendant facing potential tort liability for malpractice, or a supplier of defective components facing a suit arising out of the buyer's business disruption, we may be closer to the kind of case most lawyers come across; and here the differences are much less. Just as in contract, the requirement of knowledge arises from our wish to give a potential defendant a chance to take stock and think before committing himself, so the same can be said of many torts. Before putting himself into the position of a potential tortfeasor, a person—for example, the professional just mentioned—has the right to assume that he is not facing risks of which he has no reason to be aware.[57] Again, the issues arising out of a supply of defective goods which dislocate the plaintiff's business are not dissimilar to those engendered by, say, damage to those selfsame goods in the plaintiff's hands.

Thirdly, it must be remembered that many cases of tort do in fact arise from a choice by a defendant to accept responsibility for a given risk. Virtually all negligent misstatements are a case in point, as are tortious liabilities arising out of professional engagements such as those of attorneys or accountants. And here, where tort is in any case much more similar to contract than most lawyers would care to admit, the reasoning applicable to contract is applicable just as much to tortious liability.

A final argument in favor of excluding *Hadley v. Baxendale* from tort suits arises from the important point that the incidents of various torts differ more than those of breaches of contract. Whereas all breaches of contract can with some plausibility be lumped together and treated similarly for remoteness purposes—the defendant promised to do something and then did not do it—the same does not go for all torts.[58] In particular, there is little doubt that while torts involving inadvertent wrongdoing, such as negligence, nuisance, or strict prod-

57. *See* Evra Corp. v. Swiss Bank Corp., 673 F.2d 951, 958 (7th Cir. 1982) ("The amount of care that a person ought to take is a function of the probability and magnitude of the harm that may occur if he does not take care. If he does not know what that probability and magnitude are, he cannot determine how much care to take." (citation omitted)).

58. For example, Anglo-American law does not generally differentiate for remoteness purposes between deliberate and inadvertent breaches of contract. Interestingly enough, other systems do make such a distinction. *Compare* PRINCIPLES OF EUROPEAN CONTRACT LAW art. 9.503 (Ole Lando & Hugh Beale eds., 2000), *with* LA. CIV. CODE art. 1996 (West 1987) ("An obligor *in good faith* is liable only for the damages that were foreseeable at the time the contract was made." (emphasis added)). Perhaps surprisingly, there exists California authority which similarly differentiates be-

ucts liability, are subject to foreseeability limitations on recovery of consequential losses, the same does not necessarily go for torts involving dishonesty, such as deceit. Here, at least under the prevailing rule in England,[59] the defendant is liable for all losses directly resulting, whether or not those losses were foreseeable at all. It follows that even if the *Hadley v. Baxendale* limitations were held applicable on principle to tort suits, they would not necessarily be appropriate to all torts.

Now, this is clearly true. Nevertheless, it is easy to see that this is not a reason arbitrarily to limit *Hadley* to contract cases. Far from it, it merely means that, if *Hadley* is applicable to wrongs generally, certain types of wrong will have to be excepted. It is perfectly possible, in other words, to have a principle along the following lines: in wrongs generally, a wrongdoer is not liable for a loss that he could not have foreseen in the light of the information available to him, but that (if it is felt that fraudulent defendants should be treated differently) this will not apply to where it is shown that he has been guilty of deliberate or fraudulent wrongdoing.

B. *Arguments in Favor of a Common Standard*

So far I have argued that the arguments in favour of the orthodox "contract-only" view do not hold water. More importantly, however, it is suggested that the arguments against them, and in favour of a common standard, are even stronger. Two in particular standout.

The first concerns the phenomenon of concurrent liability in contract and tort. It must be remembered that there is nothing necessarily unusual about a person facing parallel liability in both contract and tort on the same facts. In a few situations this has always been the case: carriers, warehousemen, and other bailees for reward, negligently damaging goods come to mind. Similarly, a commercial buyer of dangerous goods may have parallel causes of action under the merchantability provisions of sales law[60] and also on the basis of negligent failure by the seller to warn, or for that matter ordinary negligence law.[61] But, rather more importantly, in recent years the same

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tween deliberate and inadvertent breaches of contract. *See* Overstreet v. Merritt, 200 P. 11, 14–17 (Cal. 1921).

59. *See, e.g.*, Smith New Court Sec. Ltd. v. Citibank N.A., [1997] 1 A.C. 254, 264–67, 281 (H.L. 1986). *But see* RESTATEMENT (SECOND) OF TORTS, § 548A (1965) (stating that in order for losses to be recoverable they must be "reasonably expected to result for reliance"); PROSSER AND KEETON ON THE LAW OF TORTS 767 (W. Page Keeton ed., 5th ed. 1984) (stating that consequential damages must be established with reasonable certainty).

60. U.C.C. § 2-314 (2004); Sale of Goods Act 1979 § 14 (Eng.). In the English Sale of Goods Act, the obligation is now re-christened "satisfactory quality" for the supposed benefit of the unsophisticated, but it means much the same thing.

61. *See, e.g.*, Vacwell Eng'g Co. v. B.D.H. Chems. Ltd., [1971] 1 Q.B. 88 (C.A. 1969) (dangerous chemical supplied by defendant to plaintiff explodes, demolishing plaintiff's premises: seller liable under both heads).

phenomenon has begun to spread elsewhere in the law. In particular, a client suing for professional malpractice may well be able to rely either on the tort of negligence or on breach of an implied contractual duty to take care—a development that has been most marked in England,[62] but which also applies, albeit in more limited circumstances, in the U.S.[63] Indeed, even the non-client beneficiary may be in the same position, depending on the generosity of the jurisdiction concerned, as regards third-party contractual rights.[64] Now, if the orthodox theory of *Hadley* is right—i.e., that consequential losses are treated in a markedly different way in contract and tort—it must follow that in any case of concurrent liability there are not one but two measures of loss: the contractual and the tortious. Such a development would be, to say the least odd, not to mention highly unfortunate. In fact there is little sign of such a development in practice.[65] Professional malpractice—a case, incidentally, where the availability of recovery for consequential loss and damage can be one of the most important issues—is routinely regarded as one topic, not two separate ones, divided according to whether liability happens to be on a contractual or on a tort theory. It follows that there should be one measure of damages for professional malpractice, and not separate measures for its contractual and tortious varieties. Other similar situ-

62. *See* Midland Bank Trust Co. v. Hett, Stubbs & Kemp, [1979] Ch. 384 (1977) (establishing the precedent for lawyer malpractice). However, since the decision of the House of Lords in *Henderson v. Merrett Syndicates Ltd.*, [1995] 2 A.C. 145 (H.L. 1994), virtually all professionals have been subject to concurrent liability in tort, whether plaintiff's loss be physical or economic. *Henderson* itself concerned the liability of a slightly recondite type of professional, namely a Lloyd's underwriting agent. *Id.*

63. *E.g.*, Congregation of the Passion, Holy Cross Province v. Touche Ross & Co., 636 N.E.2d 503, 514–15 (Ill. 1994) (bringing malpractice claim against accountant in both tort and contract); Collins v. Reynard, 607 N.E.2d 1185, 1188 (Ill. 1992) (bringing malpractice claim against lawyer in both tort and contract). Attempts to extend liability to other professionals have been less rewarding. *E.g.*, Nielsen v. United Serv. Auto. Ass'n, 612 N.E.2d 526, 532 (Ill. App. Ct. 1993) (denying malpractice claim against direct-sell insurer); Rothberg v. Reichelt, 705 N.Y.S.2d 115, 118 (N.Y. App. Div. 2000) (denying malpractice claim against architect). However, some attempts to expand professional liability beyond mere accountants and lawyers have succeeded. *See, e.g.*, Moransais v. Heathman, 744 So. 2d 973, 983–84 (Fla. 1999) (holding engineer liable for negligent pre-purchase inspection of home); Beachwalk Villas Condo Ass'n, Inc v. Martin, 406 S.E.2d 372, 373–74 (S.C. 1991) (holding architect liable in both tort and contract).

64. *See* Hale v. Groce, 744 P.2d 1289, 1290 (Or. 1987) (holding, in respect of negligent preparation of a will, that an attorney liable to would-be legatee alternatively in tort because the would-be legatee was a third party beneficiary of the attorney's contract with the testator).

65. See the English decisions in *Banque Bruxelles Lambert SA v. Eagle Star Ins. Co.*, [1995] 2 All E.R. 769 (C.A.) and *Birmingham Midshires Building Society v. Phillips* [1998] P.N.L.R. 468; and compare the old New York case of *Kerr S.S. Co. v. Radio Corp.*, 157 N.E. 140, 142–43 (N.Y. 1927) (holding *Hadley* rule applies even if concurrent liability in contract and tort). Note, however, that in *Henderson v. Merrett Syndicates Ltd.* [1995] 2 A.C. 145, 185, Lord Goff seemingly accepted, in an obiter aside, that concurrent liability might indeed lead to differential measures.

ations should follow the same rule. The seller of goods, it is suggested, should face the same liability for consequential loss to the buyer—damage done to her other property, business losses, etc.—whether he is sued under the contract of sale, for negligence, for careless failure to warn, or even on a product liability theory.

Secondly, even where there is no concurrency of liability, it has to be remembered that what is in effect exactly the same damage may fail to be compensated on different theories—contract or tort—fairly arbitrarily according to the facts of the case and the position of plaintiff and or defendant. A prime example is personal injury, which is just as plausibly a matter of contract as of torts; for example, a buyer injured by a defective product will sue the seller under sales law, but the manufacturer under a more or less strict tort theory. But there exist any number of other instances as well. If we assume a relatively narrow scope for contractual recovery by third parties, then cases of legal, accountancy, or valuation malpractice will give rise to liabilities that are contractual or non-contractual according to whether or not the plaintiff who is suing happened to be a client of the defendant. Similarly, damage to goods caused by the fault of a carrier or bailee will be compensable in contract where the claimant was in a direct relationship with the defendant, but in tort otherwise. Again, suppose goods in transit are destroyed in a collision caused by the combined negligence of the driver of the truck carrying them and that of another driver. If the owner sues the carrying trucker, she recovers in contract: if she sues the non-carrying trucker, she succeeds in tort alone. And so on. Now, in cases such as these exactly the same comment applies as with concurrent liability. Although the traditional view of *Hadley* demands a different approach to recovery of consequential losses depending on whether the plaintiff succeeds under a contract or a tort theory, as often as not there is no sensible reason why courts should differentiate the measure of recovery on this basis. The equities are very often the same, questions of the measure of recovery for damage to goods (whether consequential losses can include loss of lucrative market) or legal malpractice (can a plaintiff sue for loss of business reputation or other indirect losses) ought to be answered the same way whatever the theory on which liability is predicated.

The third point in favor of a common standard can be simply stated. Where the point actually matters there is not much indication that courts do in fact apply the strict division between remoteness in contract and tort that prevails in theory. This has been particularly noticeable in England, where the virtual absence of the civil jury means that judges have had to articulate issues of remoteness of damage with some precision. Take, for example, an instructive 1978 product liability case where defendants sold a badly-ventilated feed hopper to a hog

farm.[66] Nuts stored in it went moldy as a result, and the farmer's hogs sickened and died after eating them.[67] The main issue was whether this consequence was too remote (it was decided that it was not). In fact, the defendants were sued under sales law. Nevertheless, interestingly enough all three members of the Court of Appeals agreed, with an admirable degree of common sense, that it should make no difference to the question of remoteness whether the defendants were liable in contract or tort (though it must be admitted that their reasoning on the matter was somewhat unsatisfactory).[68] Since then, in two straightforward tort decisions defendants liable for negligent damage to a house have been exonerated for, in one case, further damage caused by an influx of squatters while the home was empty[69] and, in the other, consequential theft of the homeowner's belongings.[70] The ground in both decisions was that these losses were too remote; and although in neither case are the judgments a model of clarity, it is clear that in both cases the degree of foreseeability required by the court was a good deal more than would normally be required under the law of negligence, and that in practice, a test indistinguishable from *Hadley* was being applied.[71] Again, in a series of professional malpractice cases (which in England today are invariably brought in contract and tort in the alternative) the courts have pretty consistently applied *Hadley v. Baxendale* criteria to questions whether particular heads of consequential loss are too remote.[72] Additionally, there exist other examples of the same phenomenon.[73]

66. H Parsons (Livestock) Ltd. v. Uttley Ingham & Co., [1978] 1 All E.R. 525 (C.A. 1977).

67. *Id.* at 525.

68. *Id.* at 534. The majority in the three-judge court solemnly said that the difference in the degree of foreseeability under *Hadley* and that required to create liability in negligence was semantic and not real. *See id.* at 541. This statement, with respect, is palpably false. Lord Denning M.R. took a different line. He would have applied *Hadley* to economic loss and the more generous negligence standard to other damage. *Id.* at 534. Interestingly, Lord Denning's application of *Hadley* reflects the position in sales contracts governed by the Uniform Commercial Code. *See* U.C.C. § 2-715(2) (2004). However, it is difficult on principle to see why the distinction should be drawn at all.

69. Lamb v. London Borough of Camden, [1981] 2 All E.R. 408 (C.A.).

70. Ward v. Cannock Chase Dist. Council, [1986] 1 Ch. 546, 550 (1985).

71. *See Lamb*, [1981] 2 All E.R. at 417, 419, 421; *Ward*, [1986] 1 Ch. at 551.

72. *See e.g.*, Banque Bruxelles Lambert SA v. Eagle Star Ins. Co., [1995] 2 All E.R. 769, 841 (C.A.) (regarding valuers' liability, Lord Bingham refers to test of remoteness applicable to breach of contract or tort without differentiation); Birmingham Midshires Bldg. Soc'y v. Phillips [1998] P.N.L.R. 468. For another possible example see *Brown v. KMR Servs. Ltd.*, [1994] 4 All E.R. 385, 400 (Q.B.) (holding Lloyd's agent liable in both contract and tort).

73. For instance, in the tort of conversion the English courts have recently confirmed that where the conversion is innocent liability is limited to damage foreseeable on effectively the same basis as *Hadley v. Baxendale—i.e.*, to losses generally foreseeable, or losses of which the defendant was on notice. *See, e.g.*, Kuwait Airways Corp. v. Iraqi Airways Co., [2002] 2 A.C. 883, 1097–98 (H.L).

In the U.S., matters are, as usual, less straightforward.[74] Apart from anything else, it is as often as not that a jury be given an issue whether a given head of consequential loss is foreseeable enough to be recoverable, and with juries merely instructed to find whether that head was foreseeable to the defendant, or presented with some other equally unfocused question, it is normally not clear which foreseeability test—the contractual or the tortious—is being applied.[75] Nevertheless, it is possible to occasionally find examples of the same process that goes on in England. One notable case in the Seventh Circuit can provide the flavor. In *Evra Corporation v. Swiss Bank Corporation*,[76] a bank was sued in tort for failing to make a payment on time, with the result that the plaintiff lost the benefit of a very profitable ship charter.[77] Having discussed *Hadley* at length, Justice Posner said that even though the case was brought on a tort theory of recovery, there was essentially no difference between it and a contract action. Given the bank's lack of knowledge of the plaintiff's situation, it made no sense within the *Hadley* criteria to make it compensate the plaintiff for its loss, and the judge duly decided accordingly.

III. CONCLUSION

There is little doubt that historically the 'reasonable foreseeability' criterion in *Hadley v. Baxendale* was thought of as a fairly general damages limitation exercise whose chief function was to prevent liability for consequential loss getting out of control, and that it was only somewhat later that lawyers got the idea that there should be a fundamental cleavage between tort and contract. The aim of this article has been to show that, despite what has since become modern orthodoxy, the arguments against applying *Hadley* to non-contractual claims do not stand up. The way should therefore be open to regard *Hadley* as what it was always intended to be: a general rule applying to all forms of compensation for non-deliberate damage, whatever the formal source of the defendant's liability.[78] Whether courts will explicitly accept my common sense proposition remains, of course, to be seen.

74. In Louisiana there has been an explicit melding of contract and tort. *See, e.g.*, Pitre v. Opelousas Gen. Hosp., 530 So. 2d 1151, 1161 (La. 1988). But this is a civil law jurisdiction, and the basis was the incorporation by analogy into delict of section 1996 of the Louisiana Civil Code, which on its wording deals only with contracts, because there seemed no codal provision directly applicable. *Id.*

75. *E.g.*, McDowell, *supra* note 40, at 295.

76. 673 F.2d 951 (7th Cir. 1982).

77. *Id.* at 955–60.

78. So as not to make this Essay too long, I have not dealt with other forms of liability for wrongs, such as breach of trust. The traditional view in England is still that common law rules of remoteness, and hence *Hadley v. Baxendale*, do not apply to breach of trust actions. *See, e.g.*, Target Holdings Ltd. v. Redferns, [1996] 1 A.C. 421, 434, 438–39 (H.L. 1995). On the arguments I have advanced, this raises the same difficulties as the blanket exclusion of *Hadley v. Baxendale* from tort suits. Indeed, there is some sign that times may be changing, at least with regard to suits against