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Justice Edelman in *Moore v Scenic Tours* explained that damages for "mental harm" arising from breach of contract fall into three broad categories:

1. **Pain and suffering** resulting from physical injury caused by breach;
2. **Vexation and discomfort** resulting from physical inconvenience due to breach;
3. **Distress or disappointment** where the contract is specifically for pleasure or relaxation.

The underlying principle is that in these categories, unlike most commercial contracts, the promisor is taken to have assumed the risk of liability for such distress as part of the contractual bargain.

Practical Examples

- **Holiday and Leisure Contracts:** Where a cruise or holiday is not as promised, damages for disappointment may be awarded. For example, in *Moore v Scenic Tours*, the plaintiff was awarded damages for distress when a luxury river cruise was substantially replaced by uncomfortable bus journeys.
- **Contracts for Freedom from Molestation:** If a contract is for a restraining order and it is negligently obtained, damages for resulting anxiety or distress may be available.

Limits and Policy Considerations

- These damages remain exceptional and are only awarded where loss of enjoyment or peace of mind is a central object of the contract.
- Attempts by service providers to exclude such liability (e.g., via exclusion clauses) are often ineffective, particularly in the context of consumer contracts due to statutory protections such as the Australian Consumer Law.
- Damages are not awarded for mere disappointment with commercial outcomes or for loss of reputation except in rare circumstances where it was part of the contractual purpose.

Week 4 - Compensatory Damages for Breach of Contract (2/2)

Limitations on Compensatory Damages in Contract

- Contractual damages are available as of right (i.e. will always get at least nominal damages) subject to three relevant limitations:

1. **Causation:** D must have caused P's loss.
2. **Remoteness:** P's loss must not be too remote.
3. **Mitigation:** P must mitigate her loss.

Causation

The plaintiff must prove that the defendant's breach was a cause of the loss suffered. The test for causation in contract is the "**but for**" test which asks the question - would the loss have occurred **but for** the defendant's breach? (*Alexander v Cambridge Credit)*

Common Sense and New Intervening Acts (NIA): Where there are multiple possible causes, or a new intervening act (by a third party or the plaintiff themselves), the test is *but for* **plus common sense**. The court will determine as a matter of common sense, if the defendant's breach is still a sufficiently proximate cause, or if the chain of causation been broken (Alexander v Cambridge)

- In *Alexander v Cambridge Credit*, the majority found that, as a matter of common sense, an intervening economic downturn was the true cause of the losses—not merely the auditor's breach.
- This approach is generally stricter in contract than in tort.

Policy and Remoteness:

Some judges (see McHugh J in *March v E & M H Stramare* (1991) 171 CLR 506, in tort) have suggested that the 'common sense' aspect is really a policy judgment—sometimes overlapping with remoteness. In this view, courts may treat the question of causation as entangled with the question of whether losses are too remote.

Alexander v Cambridge Credit (1987) 9 NSWLR 310 per McHugh JA

Facts:

- The defendant auditors failed to properly audit the plaintiff company in June 1971. Had they done so, the company would have gone into receivership at that point.
- Instead, the company continued trading and suffered additional losses during a major economic downturn (1973–74).
- By 1974, when the company was finally placed in receivership, it had suffered an extra $145 million in losses.

Issue:

Whether the additional losses suffered during the economic downturn were caused by the auditor's breach, or whether the downturn was a new intervening act breaking the chain of causation.

Reasoning:

- **"But for" Test:**
  The starting point is counterfactual. If the auditors had performed their job, the company would have gone into receivership in 1971 and would not have incurred the later losses. On a simple "but for" analysis, the breach caused the loss.
- **Common Sense Test:**
  McHugh JA (with Mahoney JA agreeing) added a further layer: for new intervening acts, the test is "but for **plus common sense**." As a matter of common sense, the true cause of the additional loss was not the audit failure but the subsequent economic downturn, which was a supervening event.
  Therefore, the auditors were not liable for the post-1971 losses. (Glass JA dissented.)
- **Policy:**
  The "common sense" qualification operates as a limitation—particularly in contract law—on the extent of liability for breaches, especially where supervening events play a significant role.

Development:

- Later, in *March v E & MH Stramare* (a negligence case), McHugh J took a different approach, suggesting that questions about NIAs are policy questions about remoteness rather than causation in fact. Here, he argued such issues should be seen as "cause in law"—i.e., does the NIA render the loss too remote?

Remoteness in contract

The orthodox test for remoteness in contract in Australia is the two-limb test from *Hadley v Baxendale* . Damages are recoverable for (1) losses arising naturally (first limb) and (2) losses within the contemplation of both parties with actual knowledge (second limb).

1. **First Limb (Ordinary Losses):**
    - Damages are recoverable for losses that arise *naturally*, according to the usual course of things, from the breach.
    - This is an objective test: would a reasonable person in the defendant's position have foreseen this kind of loss as a probable result of breach?
    - *Authority*: Hadley v Baxendale, Victoria Laundry.
2. **Second Limb (Special Losses):**
    - Damages are also recoverable for any *special* losses that, while not arising naturally, were in the contemplation of both parties at the time of contracting.
    - This requires actual knowledge: the defendant must have been aware of the special circumstances giving rise to the risk of that loss when the contract was made.
    - *Authority*: Hadley v Baxendale, Victoria Laundry.

Key nuances:

- The "kind" or "type" of loss must be foreseeable, not the specific manner or extent (Victoria Laundry, The Heron II (UK)).
- The test is applied at the time of contract formation, not at breach.
- In Australian law, the courts have emphasised that contract remoteness is stricter than in tort (*e.g.*, Alcatel Australia, Alexander v Cambridge Credit).

Market Gloss or assumption of responsibility.

In the UK, *Transfield v Mercator* introduced an "assumption of responsibility" gloss in certain circumstances (e.g., established market practice). However, this approach has not been adopted in Australia, and its status remains uncertain. Unless the facts suggest a similar market understanding, Australian courts continue to apply the *Hadley v Baxendale* test.

Hadley v Baxendale

Facts

- The plaintiffs operated a mill, the main crankshaft of which broke, bringing operations to a halt.
- The only way to repair the shaft was to send it to engineers who could fabricate a replacement. The plaintiffs contracted Baxendale, a carrier, to deliver the broken shaft for duplication.
- There was a significant delay in the delivery caused by Baxendale.
- As a result, the mill was unable to operate for an extended period, and the plaintiffs claimed damages for lost profits due to this downtime.

Procedural History

- Plaintiffs sued Baxendale, claiming the lost profits arising from the extended shutdown of the mill due to the delay.

Issue

- Was the carrier (Baxendale) liable for the lost profits suffered by the mill during the delay, or were those losses too remote?

Legal Principles / Rule

- **Remoteness in contract**: Hadley v Baxendale is the foundational authority for the rule that damages for breach of contract are subject to limits of remoteness, i.e., not all consequences of a breach are compensable.
- **Alderson B articulated the classic two-limb test:**
    1. **First Limb:** Damages may be recovered for losses that "arise naturally, i.e. according to the usual course of things, from such breach of contract itself." These are losses imputed to any reasonable person in the defendant's position.
    2. **Second Limb:** Damages may also be recovered for losses "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," if special circumstances were known to both parties. These losses require actual knowledge by the defendant at the time of contracting.

Application

- In this case, the loss of profits did not arise "naturally" in the ordinary course of events for a carrier. The ordinary carrier would not expect, without being told, that the delay in delivery would stop all operations at the mill.
- The plaintiffs did **not communicate** the special circumstance—that the mill would be shut until the shaft was returned—to the carrier at the time of contracting.
- **Thus, the loss was not within the reasonable contemplation of both parties** at the time the contract was made.

Reasoning

- The case's normative basis is to incentivize parties to disclose unusual risks so that the parties can contract for them. If a risk is out of the ordinary, the party exposed should have the chance to adjust the terms (e.g., increase price, insert a liquidated damages clause, or refuse the contract).
- Baron Alderson noted that if the carrier had known about the special circumstance, he might have taken more care, charged more, or declined the job.
- The rule therefore reflects both fairness to defendants (who can plan for ordinary risks but not unusual, undisclosed ones) and economic efficiency by encouraging communication and risk allocation.
- The transcript also highlights how the rule particularly protects certain classes of defendants, such as carriers, who "do not know the businesses of all their customers." Had the contract been with another miller (with shared commercial knowledge), expectations might differ.

Victoria Laundry (Windsor) Ltd v Newman Industries [1949] 2 KB 529

Facts

Victoria Laundry operated a commercial laundry and dyeing business. They purchased a large boiler from Newman Industries to expand their business. Newman delayed delivery by about five months. Because of the delay, Victoria Laundry lost:

- Ordinary profits from its regular business (laundry and dyeing work)
- Additional profits from especially lucrative dyeing contracts that were available during the period of delay

Victoria Laundry sued for both categories of lost profits.

Issue
Are both categories of lost profit recoverable, or are the especially lucrative contracts too remote under the principles of contract damages?

Decision
The Court of Appeal held that Victoria Laundry could recover the ordinary lost profits (first limb), but not the additional profits from the especially lucrative dyeing contracts (second limb).

Reasoning

- The Court (Asquith LJ) applied and refined the two-limb rule from *Hadley v Baxendale*:
  - **First limb:** Losses that arise "naturally" in the usual course of things (imputed to any reasonable defendant)—these are recoverable. Here, it was foreseeable to any boiler supplier that late delivery would cause loss of ordinary business.
  - **Second limb:** Losses that arise from special circumstances only if those circumstances were communicated to the defendant at the time of contracting (actual knowledge)—not recoverable unless specifically made known. The especially lucrative dyeing contracts were unusual and had not been disclosed to Newman Industries.
- The distinction is between "ordinary" profits (which are presumed within the contemplation of the parties) and "special" profits (which require actual knowledge by the defendant).
- The purpose of this distinction is to allow parties to allocate risk at the time of contracting. If special risk is communicated, the defendant can decide whether to contract or adjust the terms.

Transfield Shipping v Mercator Shipping Inc (The Achilleas) [2008] UKHL 48; [2009] 1 AC 61

Facts

- The owners of the ship, The Achilleas, chartered it to Transfield Shipping, with a fixed date for return (2 May).
- The owners had arranged a highly lucrative follow-on charter at $39,500 per day, due to start 8 May.
- Transfield returned the ship late (11 May). By that time, the market had dropped, and the follow-on charter had to be renegotiated to $31,500 per day.
- The owners lost over $1.3 million in profits on the follow-on charter as a result.
- Owners sought to recover the full loss of profit for the 191-day charter.
- Transfield argued they were only liable for the lower value during the late delivery period ($158,301), citing an industry understanding that charterers are only liable for losses during the period of late delivery, unless specifically told otherwise.

Issue

- Is Transfield liable for the full loss of profit from the entire follow-on charter (over $1.3 million), or only for the limited loss during the actual late period ($158,301)?
- More broadly: what is the correct test for remoteness in contract? Is it a matter of what losses are foreseeable, or what risks the parties actually assumed?

Decision

- The House of Lords found in favour of Transfield (the charterer).
- Transfield was only liable for the loss during the late delivery period, not the entire loss from the follow-on charter.

Reasoning

- **Two approaches emerged in the Lords:**
  - **Lord Hoffmann (with Lord Hope and Lord Walker):**
    - Reframed the test for remoteness: damages should be limited by what risks the parties are objectively taken to have assumed at the time of contracting ("assumption of responsibility"), not merely what is foreseeable.
    - All contractual obligations, including secondary ones like damages, are voluntarily undertaken by reference to the objective intentions of the parties.
    - It would be wrong to hold a party liable for risks which, in the relevant market context, parties would not reasonably be considered to have assumed.
    - Here, the market understanding was that a late charterer is liable only for losses during the late delivery period, unless told of special risks.
    - **Insight:** This approach narrows the traditional "reasonable foreseeability" test, adding a gloss of market context and party intention.
  - **Lord Rodger and Baroness Hale (with whom Lord Walker also agreed):**
    - Preferred to resolve the case within the traditional Hadley v Baxendale framework.
    - Normally, loss of follow-on charter profits would be within the first limb, but because of the extremely volatile market, the extent of loss was not foreseeable.
    - The judges were criticised for focusing on the extent, rather than the kind, of loss as being unforeseeable—a departure from the traditional test (which requires only that the *type* of loss be foreseeable).
- The arbitrators, trial judge, and Court of Appeal had applied the orthodox approach and found for the owner. The House of Lords reversed this, focusing on party intention and market practice.

Insights/Notes

- **Not Australian law:** The case is persuasive but not binding in Australia. The High Court has not yet adopted the "assumption of responsibility" test.
- **Uncertainty in the law:** The case highlights uncertainty about whether the orthodox Hadley v Baxendale test still governs, or whether remoteness now also requires proof of assumed responsibility for the risk in question.