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The House of Lords in *Transfield Shipping Inc v Mercator Shipping Inc* [2008] UKHL 48; [2008] 3 WLR 345 re-considered the law relating to remoteness of damage in the law of contract. The case signals a narrower approach to the recovery of damages, although the precise ambit of the decision is unclear. It is, however, clear that it is no longer sufficient simply to show that the loss which has been suffered is a reasonably foreseeable consequence of the breach. In deciding whether or not the loss is recoverable, it may be important to ask whether or not the defendant accepted responsibility for the loss in respect of which the claim has been brought. The expectation of the market would also appear to be an important factor to take into account when deciding whether the defendant should be held responsible for the loss which has been suffered.

A charterer of a vessel redelivered the vessel late and, as a result, the owners of the vessel had to agree a reduced rate of hire for the follow-on time charter. They claimed that their loss amounted to \$8,000 per day for the duration of the follow-on charter (which was 191 days). Thus they claimed \$1,364,584 in damages. The charterers submitted that their liability was confined to the difference between the market and the charter rates of hire for the nine days during which the owners were deprived of the use of the ship. On this basis damages amounted to \$158,301.17. The House of Lords held that liability was confined to the latter figure. While they agreed in the result, the reasoning of their Lordships differed in significant respects so that it is no easy task to identify the ratio of the case.

Lord Hoffmann and Lord Hope attached importance to the question whether or not the defendant has, objectively, assumed responsibility for the loss in question. Lord Hoffmann in particular sought to transplant the approach adopted in *South Australia Asset Management Corp v York Montague Ltd* [1997] AC 191 into the law of contract more generally. Thus, for him, it was important to decide whether the loss for which compensation is sought is of a 'kind' or a 'type' for which the contract-breaker ought fairly to be taken to have accepted responsibility. On the facts he held, having regard to the expectations of the market as found by the arbitrators who initially heard the case, that contracting parties would not have considered losses arising from the loss of the following fixture to be a type or kind of loss for which the charterer was assuming responsibility.

Lord Hope also gave a central role to the idea that the defendant must have assumed responsibility for the loss in question. Thus he stated that the 'critical question' was whether the parties 'must be assumed to have contracted with each other on the basis that the charterers were assuming responsibility for the consequences of' the loss of the follow-on charter. And, importantly, he added that assumption of responsibility is 'determined by more than what at the time of the contract was reasonably foreseeable.' In his view the charterers had not assumed responsibility for any follow-on charter which the owners concluded because they could neither control that loss nor quantify it. It was not, in his judgment, sufficient that they knew 'in general and on open-ended terms' that there was likely to be a follow-on fixture.

Lord Rodger of Earlsferry did not find it necessary to explore the issues arising out of *South Australia Asset Management Corp*, nor to consider the role, if any, of assumption of responsibility in delimiting the scope of liability. In his view, the loss suffered by the owners was not the 'ordinary consequence' of the breach of contract. The loss arose as a result of the 'extremely volatile market conditions' which could not have been reasonably foreseen as being likely to arise out of the delay. The difficulty with this approach is that what was not foreseen was the extent of the loss, rather than its nature. As Lord Rodger observed, 'the extent of the relevant rise and fall in the market within a short time was actually unusual.' The problem which this approach creates is that the law does not generally require the parties to foresee the extent of the loss that has been suffered by the innocent party; rather, the law requires that the nature or the kind of loss be reasonably foreseeable. In the present case, the kind of loss (the loss of a subsequent fixture) was reasonably foreseeable and so it could be said that it should have been recovered by the owners.

Lord Walker also distinguished between the loss of a subsequent fixture and the particular loss which the owners had suffered on the facts of the case. Thus he concluded that it was open to the arbitrators to decide that it was not unlikely that the delay would cause the owners to miss a subsequent fixture but that 'it did not follow...that the charterers were liable for an exceptionally large loss (measured by the entire term of the fixture) when the market fell suddenly and sharply.' In his judgment the parties had not contracted on the basis that the charterers would be liable for 'any loss, however large, occasioned by a delay in re-delivery in circumstances where the charterers had no knowledge of, or control over, the new fixture entered into by the new owners.'

Baroness Hale also expressed her doubts about the wisdom of incorporating into the law of contract the principles set out by the House of Lords in *South Australia Asset Management Corp*. She therefore decided the case 'on the narrower ground identified by Lord Rodger.' Thus she concluded that the 'parties would not have had this particular type of loss within their contemplation.' In her judgment, the parties would have expected that the owner would be able to find a use for the ship even if it was returned late and that 'it was only because of the unusual volatility of the market at that particular time that this particular loss was suffered.'

It is no easy task to discern the ratio of this case. Lord Rodger and Baroness Hale did not support the analysis adopted by Lord Hoffmann. The approach of Lord Hope is similar to that adopted by Lord Hoffmann. Lord Walker's analysis is more difficult to discern. He found the analogy with *South Australia Asset Management Corp* to be 'helpful' but stopped short of positively endorsing it in a contractual context. It therefore cannot be said that it is necessary to show that the defendant has accepted responsibility for the kind of loss in question before the defendant can be held liable for that loss. A defendant who has assumed responsibility for the loss will ordinarily be liable for it but it does not follow that a defendant who has not assumed responsibility for the loss cannot be held liable for it.

The approach of Lord Rodger and Baroness Hale (and, possibly, Lord Walker) is to adopt a narrower approach to the definition of the 'kind' of loss (or to display a greater willingness to take account of the extent of the loss when deciding whether or not it is recoverable). The difficulty with this approach is that it does not provide clear guidance as to the circumstances in which a loss is recoverable and when it is not. Two points may, however, help to reduce the uncertainty. The first is that the knowledge of the parties at the time of entry into the contract is clearly an important factor. Where there is limited knowledge of the extent of the loss and the ability of the innocent party to control the loss is limited, it is likely to be more difficult to establish that the loss is recoverable. Second, it is likely that the courts will pay careful attention to the expectations of the market in deciding whether or not the loss is recoverable. On the facts of the case, the general understanding of the shipping market was that liability was restricted to the difference between the market rate and the charter rate for the overrun period. This was a critical factor in persuading the House of Lords to conclude that the loss was not recoverable.

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In *Robertson Quay Investment Pty Ltd v Steen Consultants Pte Ltd* [2008] 2 SLR 623, [2008] SGCA 8, the Singapore Court of Appeal examined the law relating to remoteness of damage in both contract and tort in some detail. The case establishes a number of points of importance.

First, the court affirmed (at [55]) that there is 'no doubt' that the rule in *Hadley v Baxendale*, as restated by Asquith LJ in *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd* [1949] 2 KB 528, represents the law relating to the remoteness of damage in contract in Singapore. While the court acknowledged that there is a difficulty in ascertaining the precise extent to which a kind of damage must be foreseeable, the principles underlying the rule in *Hadley* were sound.

Second the court confirmed that the remoteness test in contract is not the same as the remoteness test that is applicable in the law of tort, in particular the tort of negligence. There is a difference in this respect between a test based on reasonable contemplation of loss (the test which applies to a contractual claim) and reasonable foresight in the tort of negligence. That is to say, the rule in contract is narrower than the rule applicable in the tort of negligence. One of the reasons for this is that the parties to a contract have the opportunity to disclose to one another the losses that they may suffer in the event of a breach, whereas there is typically no such opportunity in a tort claim. This being the case, a contracting party who had the opportunity to disclose an unusual loss but did not do so is not well placed to recover that loss from the other party.

Third, the court considered the scope of the first limb of the rule in *Hadley*. Loss which falls within the first limb of the rule in *Hadley* is loss which ought to be 'well within the reasonable contemplation of all of the contracting parties'. It is a rule which does no violence to the bargain of the parties because in all probability the parties would have reached such an agreement had they thought about it.

Fourth, the second limb of *Hadley* deals with losses which are not, by their nature, within the reasonable contemplation of the contracting parties. But it only renders them liable for such losses where they had actual knowledge of the loss in question. If the parties, armed with such actual knowledge, did not make express provision in their contract for what was to happen in the event of a breach of that contract resulting in 'extraordinary' or 'non-natural' damage, then they must be taken to have agreed that should such damage occur, the contract-breaker would be liable for such damage.

Finally, the Court of Appeal concluded that the two limbs of the rule in *Hadley* are wholly consistent with, and give effect to, the contract as an agreement. The link between the remoteness rules and the agreement of the parties also serves to distinguish the rules in contract from those in tort.

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In *M & J Polymers Ltd v Imerys Minerals Ltd* [2008] EWHC 344 (Comm) Burton J held that a take or pay clause could be a penalty clause, although on the facts of the case he held that it was not penal because it was commercially justifiable and did not have the predominant purpose of seeking to deter a breach of contract.

The defendants committed a repudiatory breach of a contract for the supply of chemicals. The claimant supplier accepted the repudiatory breach and brought a claim for damages. The contract contained the following clauses:

5.3 During the term of this Agreement the buyer will order the following minimum quantities of Products...

5.5 Take or pay: the Buyers collectively will pay for the minimum quantities of Products as indicated in this Article....even if they together have not ordered the indicated quantities during the relevant monthly period.'

One of the issues in the litigation was whether or not the take or pay clause could amount to a penalty clause. Burton J held that, as a matter of principle, the rule against penalties might apply to a take or pay clause but that such a clause was 'not the ordinary candidate for such rule.' The basis for his conclusion that it did potentially fall within the scope of the rule was his finding that the obligation under Article 5.5 could only arise in a case where there had been a breach of the obligation to order the minimum quantity under Article 5.3. As he pointed out, if the minimum quantity had been ordered, the price for these goods would be due irrespective of Articles 5.3 or 5.5.

Of course, not all take or pay clauses are structured in the same way and so it does not follow from the judgment of Burton J that all such clauses potentially fall within the scope of the penalty clause rule. But, at least in the case where the obligation is triggered by a failure to purchase the minimum quantities as required by the contract, it is likely that the rule will be applicable.

However, Burton J held that, on the facts of the case, the take or pay clause did not amount to a penalty clause because it was commercially justifiable, did not amount to oppression, was negotiated and freely entered into between parties of comparable

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bargaining power, and did not have the predominant purpose of deterring a breach of contract nor amount to a provision 'in terrorem.' The negotiations had taken place between 'extremely well qualified, able and savvy commercial men against a very significant commercial background' and it could not be said that, in such circumstances, the clause was penal.