University of Tennessee, Knoxville

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Robert M Lloyd, University of Tennessee, Knoxville
Nicholas J. Chase

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RECOVERY OF DAMAGES FOR LOST PROFITS:
THE HISTORICAL DEVELOPMENT

Robert M. Lloyd
Nicholas J. Chase

A popular myth holds that *Hadley v. Baxendale* was part of a judicial trend toward limiting the power of juries to award damages for lost profits. According to this myth, pre-*Hadley* juries exercised unlimited power to award a plaintiff the damages they had suffered on account of contract breaches and other wrongs. One of the leading contracts textbooks goes so far as to say: “Prior to 1854 [the date of the Hadley opinion] there were almost no rules of contract damages. The assessment of damages was for the most part left to the unfettered discretion of the jury.”

The myth goes on to hold that the *Hadley* rule was necessary so that the industrial enterprises that were developing at the time would not be exposed to excessive damage awards if a plaintiff convinced a jury that the defendant’s breach had cost the plaintiff immense profits. Even the eminent damages scholar Professor Charles T. McCormick said that the *Hadley* rule “harmonized well with the free-trade economic philosophy of the Victorian era during which our law of contracts became systematized.”

In a law review article, Professor McCormick, the leading damages scholar of his time, gave a slightly qualified version of the same statement:

> In short, apart from a few special rules for particular types of agreements, , and some expressions to the effect that damages must be the “natural” or “necessary” result of the breach, one who failed to carry out his contract was, so far as legal theory went, liable for any and all resulting loss sustained by the other party, however unforeseeable such loss might have been.


Another scholar takes the position that courts of the time had no rules for damages but generally reached the right result on the basis of their notions of justice:

> In all the cases prior to 1854, there seems to have been, on the whole, a fair and just determination of the issue of damages in each case, without the use of any even fairly distinct rule. Each court merely applied its own notions of justice to the particular case before it, usually doing justice with only a vague statement of supposed law as to damages.

Ralph S. Bauer, *Consequential Damages in Contract*, 80 U. PA. L. REV. 687, 687-88 (1932). See also HOWARD O. HUNTER, MODERN LAW OF CONTRACTS § 14:10 (2007) (“the [Hadley] decision was a reaction to the virtually unbridled discretion of juries that had been the rule before the case. The English judges wanted control over the award of damages by jurors who might be swayed more by emotion than by reason.”)

McCormick, *supra* note 4, 19 MINN. L. REV. at 504.
These myths fit nicely with the legal realist jurisprudence that was dominant in American legal scholarship for most of the twentieth century (and even better with the critical legal studies jurisprudence that took the position that legal rules had developed as tools for maintaining the dominance of the entrenched elites). Because these myths appeared to confirm what they already believed, most American scholars accepted them with without question.

In fact, however, the law developed in quite a different way. Roman law made the first steps toward allowing plaintiffs to recover lost profits in the third century B.C.E. As the Roman economy developed, these rules on lost profit became more sophisticated and went on to become the core of the damages rules for the modern European civil law. Anglo-American law took a different course. Contrary to the myths, the common law had rigid rules limiting awards of damages, and common law judges held juries to these rules. But unlike the civil law rules, the common law rules made little allowance for the recovery of lost profits until a series of New York cases incorporated the civil law rules (as articulated by the French scholar Pothier) into American law years before the Hadley court famously relied on Pothier to postulate a rule already well known in America.

What is far more important than the fact that the Hadley rule actually migrated from the United States to Great Britain, rather than crossing the Atlantic in the other direction, is that the rule Hadley announced has become relatively unimportant as a limitation on damages. Far more important in modern law is a rule that developed alongside the Hadley rule—the rule that damages in general and lost profits in particular can be recovered only if they can be proven with “reasonable certainty.” This article will

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6 Legal realists romanticized the jurisprudence of the late eighteenth and early nineteenth century courts as wise jurists dispensing justice as determined by the facts of the cases before them, unbound by legal dogma. See, e.g., GRANT GILMORE, AGES OF AMERICAN LAW 19-64 (1977) (describing a “golden age” of American jurisprudence); KARL N. LLEWELLYN, THE COMMON LAW TRADITION: DECIDING APPEALS (1960) (describing a “grand style” of judging during this period).


8 See, e.g., Raymond S. Nickerson, Confirmation Bias: A Ubiquitous Phenomenon in Many Guises, 2 REV. GEN. PSYCH. 175, 175 (1998) (describing the tendency to give undue weight to facts that confirm preexisting beliefs and discount those that challenge such beliefs).

9 There was in fact a counter-myth. The counter-myth held that Hadley was important, not because it limited the recovery of lost profits, but for the opposite reason—that the prior law did not allow the recovery of lost profits and the Hadley decision changed the law to allow the recovery of these damages. See, e.g., GRANT GILMORE, THE DEATH OF CONTRACT 52 (1978) (“the essential novelty of the Hadley formula . . . was its affirmative statement that . . . lost profits and other consequential damages caused by a breach of a contractual duty were recoverable”). The counter-myth is closer to the truth, but it is still wrong. Contrary to what Gilmore and others said, as explained in Parts III-VI of this article, the law governing the recovery of lost profits developed independently of the Hadley rule for many years and by the time the Hadley rule became prominent, it was just a minor modification of a well-established body of rules.

10 See infra, text accompanying notes 26-34.

11 See infra, text accompanying notes 35-48.

12 See infra, text accompanying notes 74-84.

13 See infra, Part III-V.
trace that rule, showing how it developed alongside the Hadley rule and ultimately overshadowed it.

I. THE DEVELOPMENT UNDER THE CIVIL LAW

A. Recovery of Lost Profits under Roman Law

The reasonable certainty requirement, like Hadley’s foreseeability requirement, originated in Roman law. Both became important when the law began to allow recovery for lost profits. We don’t know exactly when this began. We do know, however, that the concept of recovery for lucrums cessans, or profits lost, was part of the Lex Aquilia, a plebiscite enacted in approximately 287 B.C.E. The Lex Aquilia was a compilation of private law dealing almost exclusively with tort recovery for damage done to “movable property.”

To understand why a 2,300 year-old law was such a legal landmark, we need to go back even further. The Roman legal system, like most primitive legal systems, arose as a substitute for blood feuds. The early Romans were organized on a clan basis and dealt with murder or injury to a member of the clan by taking revenge on the wrongdoer’s kin. Early on, the Romans developed (or more likely borrowed from other peoples with whom they were in contact) a device to replace the blood feud—the composition. Following a solemn ceremony, the wrongdoer made a payment of money or goods to the injured person or their kin. Originally, the essence of the payment remained retribution, but the composition was an advance because it was retribution in a form that involved fewer social costs. More important than compensating the victim and their kin was making them see that wrongdoer had also suffered and thus reducing the incentive for private vengeance. Gradually, the emphasis of this still crude but evolving legal system shifted from retribution to compensation. At first the compensation was a payment in the form of cattle, but later the payment was in money. But the system remained crude. There was no attempt to measure the damage the injured party had incurred. The payment was a fixed sum based on a schedule of wrongs.

As the Roman legal system became more sophisticated, the catalogue of rights and obligations became more complex, as did the rules of government. These rules,

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15 See infra, text accompanying notes 27-35.
19 See Jolowicz, supra note 16, at 174.

Even as late as the Twelve Tables, the law allowed punishment for the breaking of a limb by allowing the victim to inflict or have inflicted a similar injury on the perpetrator “if no agreement for compensation be made.” Jolowicz, supra, at 174 quoting a surviving fragment of the Twelve Tables.
however, had not been reduced to writing. The plebeians believed (probably correctly) that the patricians were manipulating these unwritten rules to their own advantage, so the plebeians demanded that the laws be reduced to written form. The patricians resisted, but in approximately 450 B.C., the laws of the Roman Republic were set out on twelve bronze tablets.\textsuperscript{20} These have become known as the Twelve Tables. While the laws they contained were crude and relied on magic and ritual, not only in the creation of obligations, but also as an integral part of legal procedure, they nevertheless form the foundation for our modern legal ideas. Our modern concepts of debt, contract, and civil wrongs can be traced by to the Twelve Tables.\textsuperscript{21}

Their provisions for remedies show how crude the Twelve Tables were. The penalty for the fracture of a bone was 300 \textit{asses}\textsuperscript{22} if the victim was a free man, and 150 \textit{asses} if he was a slave.\textsuperscript{23} For blows that did not result in serious injury, the penalty was 25 \textit{asses}.\textsuperscript{24} Twenty-five \textit{asses} was also the penalty for unlawfully cutting down a tree belonging to someone else.\textsuperscript{25} The size or the value of the tree did not matter, just as severity of the injury did not matter as long as it did not move the injury into a different category. The system gave the judge no discretion.

As Rome evolved from village-based agricultural economy to a commercial empire where traders and bankers played an important role, it outgrew the old legal system and new institutions developed.\textsuperscript{26} The first step toward the modern law of remedies came when the Romans began to award damages on the basis of the victim’s loss rather than a fixed schedule. This began with the Lex Aquilia, the previously-mentioned plebiscite of approximately 287 B.C.\textsuperscript{27} Among other things,\textsuperscript{28} the Lex Aquilia

\begin{footnotes}
\item[20] See JOLOWICZ, \textit{supra} note 17, at 11-12.

Scholars don’t agree as to how much of the story of the XII Tables is history and how much is myth, but the basic story is that the plebeians believed that the magistrates were manipulating the unwritten customary law of Rome to favor the patricians. A tribune of the plebeians proposed that five men be elected to draw up a code of law so that plebeians could have concrete provisions they could point to when they thought their rights were being violated. The patricians successfully opposed the project for eight years, and when they were finally forced to accede to the drafting of a code, they delayed it further by sending an embassy to Greece to study the laws of Solon. JOLOWICZ, \textit{supra} note 17, at 11. (Most scholars doubt the embassy actually went to Greece. Some think it went to the Greek colonies of Sicily or the southern Italian mainland. See, e.g., OLGA TELLEGEN-COUPEROUS, A SHORT HISTORY OF ROMAN LAW 20 (1993).)

Finally, in 451 B.C.E., ten elected magistrates drafted a code. After the assembly ratified it, the code was inscribed on ten tablets that were then placed in the marketplace. The following year the people decided the work was not complete. They elected ten new magistrates, who in turn drafted more laws, had them ratified by the people and inscribed on two additional tablets. JOLOWICZ, \textit{supra} note 6, at 11-12.

Accounts differ as to the material on which the laws were inscribed. Livy says it was bronze.

\item[21] See TIGAR, \textit{supra} note 17, at 25.

\item[22] The \textit{as} was the basic unit of coinage during the Roman Republic. In the early republic, a loaf of bread could be purchased for \(\frac{1}{2}\) \textit{as} and a liter of wine for 2 \textit{asses}. See \url{http://www.littletoncoin.com/webapp/wcs/stores/servlet/Display%7C10001%7C10001%7C-1%7C%7C learntNav%7C%7Cguide-to-ancient-roman-coinage.html} (last visited Feb. 28, 2015).

\item[23] See JOLOWICZ, \textit{supra} note 17, at 174.

\item[24] See \textit{id.} at 174-75.

\item[25] See \textit{id.} at 174.

\item[26] See TIGAR, \textit{supra} note 17, at 27-28.

\item[27] One commentator gives its date as 286. Ross, \textit{supra} note 16, 14 Tul. J. Int’l & Comp. L. at 528. Another says the Lex Aquilia is “of uncertain date, but certainly later than the XII Tables.” JOLOWICZ,
provided what may have been the world’s first system of damages to base the victim’s recovery on the value of their loss, rather than on a rigid schedule.

The first chapter of the Lex Aquilia provided: “If anyone wrongfully . . . slays a male or female slave belonging to another person, or a four-footed . . . animal, let him be condemned to pay the owner as much money as the maximum the property was worth in the year [previous to the slaying].”29 The third chapter contained similar remedies in the case where any person damaged other types of chattels “by wrongfully . . . burning, breaking or rending.”30 In the case of burning, breaking, or rending, however, the victim’s recovery was limited to the highest value within the 30 days immediately preceding the damage.31 In any of these cases, if the defendant denied liability, the payment to the plaintiff was doubled.32

The literal language of the Lex Aquilia allowed only the recovery of direct damages, but later interpretations allowed the plaintiff to recover his “interest” (interesse in Latin) in the wrongful act not having occurred.33 From this developed the idea that the plaintiff could recover consequential damages.34 One nineteenth century publication gave examples of the earliest consequential damages allowed under Roman law: “If one of a pair of mules, or of a team of four horses, or one of twins, or of a band of comedians, is killed, account must be taken not only of the value of the person killed, but also of the depreciation of the rest.”35

As the Roman commerce developed, the law of Rome developed along with it, becoming very solicitous of the interests of merchants.36 Eventually, the consequential damages recoverable came to include future profits the plaintiff lost because of the

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supra note 17, at 173. And still another says: “The date of the *lex Aquilia* is not certain but what evidence there is points to 287 B.C. and there is no positive reason for assigning the statute to any other time.” ALAN WATSON, THE LAW OF OBLIGATIONS IN THE LATER ROMAN REPUBLIC 234 (1965) (footnote omitted). He also expresses the belief that it was at least in part a codification of existing legislation. See id.

28 The Lex Aquilia is also notable because it did away with the need to fit the loss into one of the strict categories prescribed in the Twelve Tables. It allowed a plaintiff to bring an action in datum injuria datum, literally “damage given without right.” Ross, supra note 16, 14 TUL. J. INT’L & COMP. L. at 528. 29 As quoted at Ross, supra note 16, 14 TUL. J. INT’L & COMP. L. at 529.

30 Ross, supra note 14, 14 TUL. J. INT’L & COMP. L. at 529 quoting DIG. 9.2.27.5 (Ulpian, Edict 18, reprinted in BRUCE W. FRIER, CASEBOOK ON THE ROMAN LAW OF DELICT 6 (Bruce W. Frier trans., 1989).

31 See W.W. BUCKLAND, A TEXTBOOK OF ROMAN LAW FROM AUGUSTUS TO JUSTINIAN 585 (3D ED. (STEIN) 1963).

32 See Ross, supra note 16, 14 TUL. J. INT’L & COMP. L. at 529.

33 See id. at 530.

As to the importance of the interpretations of Roman law by the jurisconsults, see infra, text accompanying notes 39–41.

34 See Ross, supra note 16, 14 TUL. J. INT’L & COMP. L. at 530.

See also JOLOWICZ, supra note 17, at 290 (noting that interpretations “going back at least as far as Labeo [who died c. 10 A.D.] allowed the plaintiff to include consequential damages as well.”)


Anticipating the modern law of lost profits, the Romans allowed recovery under the Lex Aquilia only if the amount of the damages could be estimated in money. See id. at 95. Cf. RESTATEMENT (SECOND) OF CONTRACTS § 352 (1989) (damages not recoverable beyond amount proved with reasonable certainty).

36 See TIGAR, supra note 17, at 27.
injury. Roman law then began dividing the damages into two categories: *damnum emergens* (damage emerging), which were the direct damages suffered by the plaintiff and *lucrum cessans* (profit ceasing), which were the profits that the breach caused the plaintiff to lose.

Like most of Roman law, these concepts did not come through judicial decisions or through legislation. Instead they resulted from the work of legal scholars known as jurisconsults. The jurisconsults (sometimes referred to simply as “jurists”) were scholars recognized as experts in their respective fields of law but without any direct legislative or judicial authority. Their writings carried great weight, so much so that for a time during the second century A.D. the opinions of certain jurisconsults were binding on judges. Much of the Roman law that eventually became the basis for the legal systems of modern continental Europe derives from the writings of the jurisconsults. This scholarly tradition continues to play an important part in the jurisprudence of civil law countries, and it is through the work of an eighteenth century successor to the jurisconsults, the previously-mentioned Robert Joseph Pothier, that much of our law on commercial damages came into the common law system.

### B. European Civil Law and Pothier

The Roman law-based legal system of modern Europe has its roots in Bologna, Italy in the late eleventh century. The first modern university developed at Bologna and its scholars made law, specifically Roman law as set out in Justinian’s Institutes, a major subject of study. Scholars from throughout Europe came to Bologna, learned Roman law, and returned home to establish universities where they themselves taught the Roman law. In this way, they made Roman law a common law of continental Europe. In some parts of the continent (e.g., Germany), the principalities officially adopted Roman law, as taught at Bologna, as their governing law. In others there was no official recognition of the Roman law, but tribunals accepted Roman law as authoritative even though it was not

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37 See **BUCKLAND, supra** note 31, at 588.
38 See id.

Professor Dawson notes that there is some doubt as to the correctness of the reports that the opinions of the jurisconsults were binding. **JOHN P. DAWSON, THE ORACLES OF THE LAW** 109-10 (1968).

40 See **CIVIL LAW TRADITION, supra** note 39, at 57.

One writer says that the jurists “could function rather like an informal but very real standing commission for law reform.” **J.A.C. Thomas, Roman Law, in AN INTRODUCTION TO LEGAL SYSTEMS** (J.D.M. DERRETT, ED. 1968).

41 See **CIVIL LAW TRADITION, supra** note 39, ch. IX.
42 See supra, text accompanying note 13. Pothier’s writings and their influence are discussed extensively in Parts III and IV, infra.
43 See infra, Parts III and IV.
44 See **CIVIL LAW TRADITION, supra** note 39, at 9.
45 See id. at 9-10.
46 See id.
Thus, in one way or another, the law of Rome became the law of Western Europe.47

In France, Robert Joseph Pothier, a professor at Orleans, published a series of studies on Roman law.49 The most important of these was his Traité des obligations, a study of the Roman law of obligations (i.e., contracts and torts).50 The drafters of the Code Napoleon adopted Pothier’s work as one of their technical guides,51 and William Evans, a London barrister, translated it into English by under the title A Treatise on the Law of Obligations, Or Contracts.52 Evans’s translation was first published in 1806, and it quickly became a standard reference work for lawyers in the United States as well as for those in England.53

With the Roman law had come lucrum cessans. Although lucrum cessans had been important in allowing merchants to recover lost profits in the commercial economy of the late Roman Empire, the agrarian economy of the Middle Ages provided little opportunity for medieval lawyers to use it this way. They did use it however. It served them as a vehicle for avoiding the usury laws. This was not something new. The Roman lawyers had come up with a clever legal fiction. Prohibited from suing the borrower for interest on a defaulted loan, they sued under lucrum cessans to recover the “loss of profit . . . that could have been made with the money lent that is foregone.” They combined this with a claim under damnum emergens for “the incurrence of costs in making the loan itself.” 54

Medieval lawyers built on this idea, and the device became so common that in 1176 Pope Alexander III wrote to the Archbishop of Genoa denouncing the practice:

47 See id.
48 Id. at 10.
50 The Roman law of obligations was essentially the law of in personam rights. For every right there was a correlative duty. According to Professor Barry Nicholas, “The [Latin] term obligation denotes sometimes the right, sometimes (like the English ‘obligation’) the duty, but more properly, it denotes the whole relationship.” BARRY NICHOLAS, AN INTRODUCTION TO ROMAN LAW 158 (1962). The great Roman jurisconsult Gaius divided obligations into two categories: ex contractu (those arising from contract) and ex delicto (those arising from delict). See id.
51 See Tigar, supra note 17, at 218.
52 See Perillo, supra note 49, 11 Tex. Wesleyan L. Rev. at 270 n.22 Professor Perillo notes that this is a truncation of the French title. See id.
53 See id.
You tell us that it often happens in your city that people buy pepper and cinnamon and other wares worth at the time not more than five pounds, promising those from whom they received them six pounds at an appointed time. Though contracts of this kind and under such a form cannot strictly be called usurious, yet, nevertheless, the vendors incur guilt unless they are really doubtful whether the wares might be worth more or less at the time of payment. Your citizens will do well for their own salvation to cease from such contracts.55

As a scholar of medieval economics points out, the justification for enforcement of the promise to pay six pounds is that “the trader is entitled to recompense for the probable loss of profit,” and therefore the pope’s letter “consequently constitutes a recognition of the title lucrum cessans.”56

What is more important, recent scholarship has shown that our modern rule allowing lost profits to be recovered only if they can be proven with reasonable certainty also has its origin in the jurisprudence of lucrum cessans:

[Beginning in the 13th Century,] lucrum cessans as foregone profits was sometimes claimed by lenders of monetary capital who wished to collect interest on their loans and thus needed to avoid the charge of usury. They had to prove that in lending funds they forewent a real and certain opportunity of profiting by having invested their capital in a given project. Two corollaries follow from that:
1) The lender (businessman or entrepreneur) in question must to claim, with certainty, a given amount of foregone profits as a result of a lost economic opportunity and/or
2) The businessman or entrepreneur exercising the claim must operate in the framework of a stationary/traditional society. This has to be the case in order to:
   a) calculate with certainty the value of lost profits. This would only be possible, assuming the absence of monopoly (itself a very improbable and unlawful market structure), were there to obtain a stationary or steady state economics system.
   b) postulate the nonexistence of a competitive environment. Obviously, were that not the case, competition would make it impossible to calculate with certainty a given foregone volume of profits.57

56 Id.
In other words, recovery of *lucrum cessans* required a level of proof that could be obtained only where the lender held near-monopoly power. If he did not a 13th century court would not permit recovery because it was not certain that profits had been lost. But, if the lender was able to meet the burden of proof, he could recover interest on the money he lent by claiming that the interest was merely profit that the money could have made if invested elsewhere. 58

The *damnum emergens/lucrum cessans* dichotomy was carried forward into the civil law and into international commercial arbitration, in both of which areas it continues to play an important part. 59

II. THE COMMON LAW DEVELOPMENT

A. The Role of the Jury

The common law principles of damages developed in quite a different way. 60 The earliest development was similar to that of the Roman law, with a rigid system of compensation emerging to replace the blood feud. Before the Norman Conquest, the Anglo-Saxon peoples developed a schedule that set the price at which a wrongdoer was required to make *bot* or compensate his victim. Professor McCormick’s treatise on damages contains an extensive list from the Law of Ethelbert, who reigned at 600 A.D. If the wrongdoer struck out an eye, the bot was 50 shillings; for striking off an ear, it was only 12. Knocking out a front tooth cost 6 shillings, but a molar was worth only a single shilling. 61

The royal courts established after the Norman Conquest generally did not have such specific rules, nor were what rules they had so uniformly followed, being for the most part rules of the common law rather than of statutes. This has led scholars to conclude that tribunals had considerable discretion in the award of damages. The most extensive study of the history of contract damages says: “Until the close of the eighteenth century, the Courts almost never discuss the principles by which the quantum of recovery

58 Id.
60 Curiously, even though the Romans ruled Britain for 350 years, the Roman law had no discernible effect on the early English law. For an interesting discussion of the possible reasons, see David A. Thomas, *The Disappearance of Roman Law from Dark Age Britain*, 1984 BRIGHAM YOUNG UNIV. L. REV. 563 (1984).
61 See MCCORMICK, supra note 6, at 22.
is to be estimated. The inquiry is not ‘How much shall be given?’ but rather, ‘Who shall make the assessment and who correct a finding alleged to be erroneous?’ As discussed below, this is likely an overstatement. The lawyers of the day were so focused on procedure that the contemporary case reports probably neglected to mention substantive issues of damages that were actually argued.

The first provisions for correcting erroneous damages assessments were crude in the extreme. Beginning in the late thirteenth century, a defendant who felt the damages assessed against him were excessive could apply for the writ of attaint. This would result in the convening of a grand jury of 24 knights, who would re-try the case. If they issued a finding of faux serement, not only would the original verdict be annulled, but, more importantly from the point of controlling the jury, the petty jury that returned the verdict would suffer a punishment that strikes modern readers as entirely out of proportion to the offense. They could be imprisoned for an indefinite time, suffer forfeiture of all their chattels, have their houses razed, their meadows plowed up, and their trees extirpated. If this was not enough, they could be condemned to perpetual infamy.

Attaint appears to have been seldom if ever granted for insufficient damages, so there must have been considerable pressure on jurors to keep the award as small as possible. The plaintiff awarded insufficient damages may not have been without a remedy, however, because it appears to have been the practice to allow such a plaintiff to obtain a non-suit and then sue again.

By the seventeenth century, attain seems to have died out. In its place, courts began to control the award of damages by the grant of a new trial in cases where the damage award offended the judge’s sense of justice. Until 1670, however, it appears to have been the practice to fine the original jury whenever a new trial was awarded.

During this time, the courts seem to have employed narrow rules for estimating the damages in the limited types of cases for which such rules were feasible. McCormick says:

By the end of the [eighteenth] century, it was clear that in England the courts would grant a new trial if the award violated some rule of

63 See infra, text accompanying note 65.
64 See Washington, supra note 62, 47 L. Q. REV. at 346.
65 See id. at 346-47.
67 Washington, supra note 61, 47 L. Q. REV. at 349. One article describes attaint as “an extraordinarily complicated and rarely used procedure.” Berman & Reid, supra note 63, at 468. Still, possibility of this extreme punishment must have weighed heavily on the jurors.
68 Washington, supra note 62, 47 L. Q. REV. at 353.
69 See id. at 350 (although attaint was not formally abolished until 1825, it almost never seems to have been brought after the beginning of the seventeenth century).
70 See id. at 359.
damages—such rules were few and chiefly confined to contracts—or if even in tort cases the court, in its discretion, considered the amount unreasonable.

Parallel with the widening of the court’s power to set aside the award was the growth of the practice of judges guiding the jury in advance toward a finding of damages in accordance with consistent standards. This is a chapter in legal history which has not as yet been written, but we know the charge or instruction of the judge was a feature of jury trials from the first. The amount of damages was a “fact” as to which the judge would have at first offered suggestions merely; but as standards of damages are worked out for the different forms of action, particularly contract actions, takes on the tone of instruction. We may be sure that this practice of advising the jury upon the measure of their award, even more than the power to change or set it aside, provided the main vehicle for the formulation of the rules and standards of damages.71

Most writers, however, have claimed that until Hadley was decided in 1854, juries had unfettered discretion in awarding damages in contracts cases.72 The Calamari & Perillo textbook was quoted at the beginning of this article.73 Richard Danzig, in his famous article on Hadley v. Baxendale, takes a similar position. He notes that Chitty’s treatise on contracts, then the leading English authority on the subject, discussed the question of damages hardly at all. He says that Chitty’s only comment on damages in the ordinary run of cases was:

When the parties have not furnished the criterion of damages by stipulating for a liquidated sum to be paid as such, it is, in general entirely the province of the jury to assess the amount, with reference to all the circumstances of the case.74

What Danzig and other scholars who have commented on the dearth of discussion of damages in contracts treatises overlook is that eighteenth century lawyers did not consider the rules of damages for breach of contract to be part of the law of contracts. Damages was considered a separate subject. Even as late as the early twentieth century, Langdell’s contracts casebook did not contain Hadley v. Baxendale (or any other damages case).75

72 See supra, note 6 and accompanying text.
73 See id.
75 See E. Allen Farnsworth, Contracts Scholarship in the Age of Anthology, 85 Mich. L. Rev. 1406, 1443 (1987). Although Hadley was often included in damages casebooks, it did not appear in any contracts casebook until 1931. See id.
The truth is that by 1847 the law of damages was so extensive that Theodore Sedgwick, a Massachusetts lawyer, could write a 571-page treatise on the subject.\footnote{THEODORE SEDGWICK, A TREATISE ON THE MEASURE OF DAMAGES (1847).} In his Introduction, Sedgwick quoted Lord Kaims’s 1767 English treatise \textit{Principles of Equity} as saying: “Damages are taxed by the jury, who give such damages, as in conscience they think sufficient to make up the loss, without regarding any precise rule.”\footnote{\textit{Id.} at 2 quoting \textsc{Henry Home (Lord Kaims), Principles of Equity} 78 (2D ED. 1767).} Sedgwick then went on to say: “It is superfluous to say, that no such arbitrary discretion is now tolerated, except in a very limited class of case, if indeed in can be properly said to exist at all.”\footnote{SEDGWICK, supra note 76, at 2.} Later in his treatise, Sedgwick said:

[I]t is now well settled that in all actions of contract, subject to the exception [for breach of promises of marriage], and in all cases of tort where no evil motive is charged, that the amount of compensation is regulated by the discretion of the court, and that the jury cannot substitute their vague and arbitrary discretion for the rules which the law lays down.

It is in fact indispensable that it should be so; the measure of damages is the gist of the remedy; the remedy is no part of the facts of the cause, while, on the other hand, it so completely controls the rights of the parties, that if any absolute discretion be given the jury over the amount of compensation, the power of the court over questions of law, would be most emphatically a barren sceptre.\footnote{\textit{Id.} at 214-15.}

A review of the cases shows that Sedgwick was right. Virtually every important American contract damages opinion from the decades immediately preceding \textit{Hadley} indicates that the court gave the jury explicit instructions as to the way damages were to be calculated.\footnote{See, e.g., \textit{Fox v. Harding}, 61 Mass. 516, 522-23 (1851) (upholding jury instructions denying profits on collateral contracts); \textit{Miller v. Mariners Church}, 7 Me. 51, 56 (1830) (upholding jury instructions denying recovery of losses which claimant could have avoided); \textit{Driggs v. Dwight}, 17 Wend. 71, 74-75 (N.Y. 1837) (upholding jury instructions allowing tenant to recover cost of moving); \textit{Bush v. Canfield}, 2 Conn. 485, 488 (1818) (upholding jury instructions on measure of damages); \textit{Bridges v. Stickney}, 38 Me. 361, 371 (1854) (new trial granted where jury instructed they could include in damage calculations losses on collateral contract); \textit{Deyo v. Waggoner}, 19 Johns. 241, 243 (N.Y. Sup. Ct. 1821) (jury verdict reversed because it improperly included consequential damages); \textit{Davis v. Talcott}, 14 Barb. 611 (N.Y. Sup. Ct. 1853) (relating detailed instructions given to the jury, explaining what items could be included in the damage calculation and how lost profits were to be calculated); \textit{Wille v. Fredericks}, 76 Mass. 357, 360 (1858) (upholding instruction that jury could take into account loss of use of land in determining damages for breach of agreement to build sea wall); \textit{Lord v. Strong}, 6 Mich. 61, 68-69 (1858) (upholding jury instructions that damages for breach of contract to carry lumber by ship were difference between contract price and price of freight on day cause of action accrued); \textit{Morrison v. Lovejoy \& Brockway}, 6 Minn. 319, 354 (1861) (granting new trial because jury instructions failed to instruct jury rent of mills should have been taken into account in calculating lost profits).}

\textit{Blanchard v. Ely}, discussed \textit{infra} in Section III. and \textit{Masterton v.}
Brooklyn, discussed *infra* in Section IV, are just two examples. In a case that reached the United States Supreme Court in 1852, two years before the Hadley decision, the plaintiff had requested eleven separate jury instructions, each pertaining a separate item of damages.\(^\text{81}\) It is not clear how long American judges had been instructing juries on the damages they were allowed to award, but there is evidence of it from the first reports of the newly independent American states.\(^\text{82}\)

delayed. The jury did as instructed, but the appellate panel held that only the cost of the repairs was allowable as damages.

A Maine case, White v. Oliver, 36 Me. 92 (1853), involved a suit for failure to pay for the construction of a house. The defendant claimed the house had not been finished and that the construction that was completed had not been completed according the specifications. The court instructed the jury that the plaintiff “was entitled to receive for the house only the balance that would remain after deducting from the contract price as much as it would cost to make the house as it should have been by the contract.” *Id.* at 616.

In another Maine case, Furlong v. Polleys, 30 Me. 491, 494 (1849) a jury verdict was set aside and a new trial granted because the jury instruction, which specified the damages for the nondelivery of hay were the difference between the contract price and the market price did not specify the place at which the market price was to be determined.

*Cf.* Wahrth v. Redfield, 11 Barb. 368, 371 (N.Y. 1851) (where defendant’s dam caused injury to plaintiff’s mill, court awarded new trial because trial judge had given improper jury instructions as to damages; court indicates that in the absence of fraud, gross negligence, or wantonness, the same damages rules apply for tort as for contract).


\(^\text{82}\) See, *e.g.*, Groves v. Graves, 1 Va. (1 Wash.) 1 (1790). This was the first-officially-reported case of the Supreme Court of Virginia. The court reversed a jury verdict that awarded damages for the failure to deliver settlement certificates, the value of which had declined drastically. The Supreme Court ordered a new trial because the jury had valued the certificates as of the date of trial, rather than as of date they should have been delivered. *Id.* at 3.

In some cases, it appears that the courts were actually looking to the jury to develop a rule of law that would be a binding precedent in future cases. For example, in 1804 Supreme Court Justice Washington, while riding circuit, tried a case in which an agent for a seller of goods delivered the goods to the buyer without receiving payment, apparently in violation of express orders. Justice Washington charged the jury:

The next question is, as to the damages? I admit the principle, that in cases sounding in damages, the amount of damages depends on the sound discretion of the jury. In cases where merely vindictive damages are sued for, the jury act without controls on this subject; because there is no legal rule by which they can be measure; and unless they are so extravagant as to induce a suspicion of improper conduct, the court will not interfere. *But in these cases, where a rule can be discovered, the jury are bound to adopt it.* That rule is, that the plaintiff shall recover so much, as will repair the injury sustained by the misconduct of the defendant; and applying this rule in the present case, what other measure of damages can be thought of, but the sum lost to the plaintiff by the violation of his orders? The sum demanded, is of no great consequence, perhaps, to either of the parties, on the score of its amount. But the question itself is important to the commercial interests of this country; in its intercourse with foreign nations. *A precedent is to be set to determine in a case like this, whether an agent is liable for a breach of orders and to what amount.*

*Walker v. Smith, 29 Fed. Cas. 56, 57 (Cir. Ct., D.Pa. 1804)* (emphasis supplied).

When the jury awarded the plaintiff what the reporter of decisions said was “a sum much inferior to the loss he had sustained,” Justice Washington overruled the plaintiff’s motion for a new trial. *Id.* The reporter paraphrases him as saying “that although he was not satisfied with the verdict, not should he have assented to it as a juror, yet the question of damages, or of interest in the nature of damages, belonged so peculiarly to the jury, that he could not allow himself to invade their province . . . .” *Id.*
that while Justice Washington alluded to the broad general principle of awarding the amount that would make the plaintiff whole, the use of these broad principles did not come into vogue until a half century later (see infra note 178 and accompanying text), so he was looking to the jury to make a narrow rule for determining the damages to be awarded when an agent delivered goods without authority.

When the South Carolina Supreme Court upheld a compromise verdict in a case involving the value of a debt denominated in continental currency, the New Jersey Supreme Court read the opinion as creating a precedent requiring similar compromises in all such cases. In Pledger v. Wade, 1 Bay 35, 1 S.C. 33 (1786), Pledger had executed a promissory note to Ely Kershaw & Co. in the amount of $18l. 19s. 9d. In February, 1780, Wade contracted to acquire this note and return it to Pledger, but the note was held in Charleston and before Wade could get possession of the note, the British invested Charleston, and it became impossible for Wade to perform. See 1 S.C. at 33. The courts did not then recognize the doctrine of impossibility (See Berman & Reid, supra note 66, 45 EMORY L.J. at 462-63) so Wade was liable on his contract. The issue was amount of damages.

The opinion does not say so explicitly, but from the context of the case, it seems clear that the note in question was payable, not in pounds sterling, but in bills of credit issued by the State of South Carolina and also denominated in pounds, shillings, and pence. For most of their existence, these bills (which were not backed by specie) traded at approximately seven South Carolina pounds to one pound sterling. See JOHN J. McCUSKER, MONEY & EXCHANGE IN EUROPE & AMERICA (1600-1775) 220-26 (1978). To finance its participation in the Revolutionary War, however, South Carolina, like most states (and the Continental Congress), began issuing huge quantities of this fiat money. The combination of the increase in the amount of state currency in circulation and the prospect that it might become valueless if the revolution failed caused the currency to depreciate precipitously. See id. In 1783, South Carolina enacted a Depreciation Act setting the value in specie that would have to be paid to discharge a debt incurred during the inflationary period April 1777 through May 1780. It contained a month-by-month table setting the ratios of specie to paper currency.

Pledger’s counsel argued that because the note in question had been issued before the period covered by the Depreciation Act, Wade was liable for the principal amount of the note plus the interest that had accrued on it through the date of the Pledger-Wade contract (287l. 11s. 8d.). See 1 S.C. at 33-34. Wade’s counsel argued that the debt on which the suit was based was the obligation to procure the note, and that had been incurred when the contract was executed, making the obligation subject to being discounted under the act. See 1 S.C. at 34. While today we would probably consider the issue a question of law for the court, this court treated it as a question of fact to be decided by the jury. See 1 S.C. 34.

On that issue, the jury returned a compromise verdict. They awarded the principal sum of “38l. 18s. 5d., the amount of money as depreciated in February, 1780 [the time the contract to acquire the note was made].” But it awarded interest in the amount of 71l. 2s. 9d. This, the reporter described as “interest on the nominal sum contended for [i.e., on the 287l. 11s. 8d. face amount of the note].”

The South Carolina Supreme Court refused to order a new trial, issuing a per curiam opinion that read in full:

As this is a case sounding in damages, and as the jury have thought proper to give a kind of equitable verdict between the parties; and as this also appears to be a hard case, we against granting a new trial.

1 S.C. at 34.

But unlike later scholars, (See, e.g., Horwitz, supra note 92, 87 HARV. L. REV. at 926) contemporary courts did not read this opinion as giving free rein to juries to assess whatever damages they thought appropriate. The New Jersey Supreme Court cited Pledger v. Wade for the proposition that “when a bond is not wholly paid off, all payments of continental money, so far as they affect principal, are to be liquidated according to the tables of depreciation; but in the payment of interest, it is to be taken as to its nominal value.” Executors of Todd v. Parker, 1 N.J.L. 54, 55 (1791). So in refusing to overturn a jury verdict, the South Carolina court in effect created a rule for calculating damages that would be binding on later juries.
It is probably true that English judges were less likely to instruct the jury on the measure of damages than were American judges, but the few cases cited for the proposition that English juries had unfettered discretion do not really support it. For example, in *Waters v. Towers*, the defendants breached a contract by failing to set up the gearing for a bobbin mill in a timely and workmanlike manner. The owners of the mill were awarded damages of 14l. for their apprentices being unemployed and 133l. for the lost profits on an oral contract to supply bobbins to a firm consisting of two of the three plaintiffs. While this opinion does show the court upholding an award of lost profits on a collateral contract, something that American courts were still a few years from doing, and while it also shows the court upholding an award that might not have passed the *Hadley v. Baxendale* test, the report does not show the jury’s award exceeding the amount supported by the evidence, nor is there any indication the jury was not instructed on the rules of expectation damages. The case report consists almost entirely of the statement of the facts, the procedural history, and the argument of the defendants’ barrister. The only opinion is a per curiam “The rule [nisi of the lower court] must be absolute.” The only other statement of the judges quoted in the opinion is Baron Alderson’s statement that the plaintiff’s testimony as to the oral contract to sell bobbins would have been sufficient evidence of the amount of the loss. Even this seems to have been made, not in response to an argument concerning the amount of the damages, but in response to an argument that the contract to supply bobbins could not be the basis for a damages award because it was not in writing.

**B. The Reluctance of American Courts to Award Lost Profits**

To understand the way the law of lost profits developed in the United States, we need to understand the jurisprudence of the early nineteenth century. American lawyers of that time were not concerned with broad general principles from which the rule for a specific case could be derived. Instead, they adhered to narrow precedents that articulated

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85 See id. at 1404.
86 See id. at 1405.
87 Id.
88 See id. Alderson’s full statement was:

> If a person undertakes to make a certain article for another, and to deliver it to him on a particular day, but fails to do so until a year afterwards, it would be most unreasonable that the latter could not recover any damage because the contract was not in writing. The existence of a contract is evidence of the probable amount of the loss sustained. Suppose the plaintiffs had said, “we should have made such and such a contract if the defendants had performed theirs,” and the jury believed the plaintiffs would have done so, that would surely have been evidence of the amount of loss occasioned by the defendant’s breach of contract.  

Id.
specific rules for specific situations. Oliver Wendell Holmes, Jr. described American law as late as 1864 as “a ragbag of details.”

We can put the blame on Blackstone. American legal thinking of that time derived primarily from Blackstone. In Blackstone’s time, and for many centuries leading up to that time, the English social structure was based on ownership of real property. So to Blackstone, law was all about property rights. And because the stability of the society depended on property rights, Blackstone was all about black-letter rules. These were not the broad general rules that guide our jurisprudence today. They were narrow rules designed to cover specific situations. As one writer put it, “the common law he was talking about was a hodge-podge of local practice and custom.”

In 1847, Sedgwick apologized for the disjointed organization of his treatise on damages, explaining that convention dictated following Blackstone's scheme of organization:

In preparing this work, my chief embarrassment has arisen from the difficulty of making a proper and scientific division of the subject. The whole arrangement of our Anglo-American jurisprudence . . . [is] so purely arbitrary and technical, that it is almost impossible to prepare a treatise on a subject as extensive as that of the measure of damages, which shall be at once useful and logically arranged. To be useful, it must, to a very considerable extent, (at all events,) conform to those arbitrary

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89 Oliver Wendell Holmes, Jr., Collected Legal Papers 301 (1881) quoted at Michael L. Rustad & Thomas H. Koenig, Taming the Tort Monster: the American Civil Justice System as a Battleground of Social Theory, 68 Brooklyn L. Rev. 1, 12 (2002).
92 See 2 William Blackstone, Commentaries on the Laws of England 2 (1766) (“There is nothing which so strikes the imagination, and engages the affections of mankind, as the right of property . . . .”). Professor Horwitz has written:

To modern eyes, the most distinctive feature of eighteenth century contract law is the subordination of contract to the law of property. In Blackstone’s Commentaries contract appears for the first time in Book II, which is devoted entirely to the law of property. Contract is classified among such subjects as descent, purchase, and occupancy as one of the many modes of transferring title to a specific thing. Contract appears for the second and last time in a chapter entitled, “Of Injuries to Personal Property.” In all, Blackstone’s extraordinarily confused treatment of contract ideas occupies only forty pages of his four-volume work.

Morton J. Horwitz, the Historical Foundations of Modern Contract Law, 87 Harv. L. Rev. 917, 920 (1974).
93 See Stewart E. Sterk, Intellectualizing Property: The Tenuous Connections Between Land and Copyright, 83 Wash. U. L. Q. 417, 419 n.4 (2005) (“Blackstone, in both his judicial opinions and his commentaries, contributed significantly to the conception of property as rigid and rule-laden.”)
divisions which are altogether independent of any scientific analysis, and very frequently are directly in conflict with logical order. Conscious of the difficulty, yet seeing no mode to avoid it altogether, I have endeavoured as far as possible, to make my treatment of the subject correspond with that which Blackstone adopted, and which subsequent writers on our law have generally followed.95

Foremost among these “subsequent writers on our law” was Chancellor James Kent, whose Commentaries on American Law, first published in four volumes in 1825-30, came to overshadow Blackstone in shaping American law.96 Like Blackstone, Kent set out specific rules that applied only in specific situations. For example, Kent did not have a chapter on the rules of contract law. Instead he had one chapter for the law of contracts of sale of personal property, one for the law of contracts of bailment, one for the law of contract of affreightment, and one for the law of contracts made by minors.97

None of these rules contemplated the award of lost profits, except to the extent that the damages formula gave some sort of recovery that would approximate the profits. For example, where a seller failed to deliver the goods contracted for and the buyer had paid no part of the purchase price, the damages were the difference between the contract price and the market price at the time and place the goods were to be delivered.98 This is basically the rule under the UCC, except that the UCC contemplates additional incidental and consequential damages.99 But if the buyer had paid the purchase price in advance, some of the caselaw held that the damages were then the difference between the contract price and the highest market price of the article between the time of the contract and the time of trial.100

Kent’s narrow rules so frustrated Oliver Wendell Holmes, Jr., who edited the twelfth edition of the Commentaries, that he groused that Kent “has no general ideas except wrong ones.”101

Justice Joseph Story’s opinion in The Lively102 was the second major cause of American courts’ failure to award damages for lost profits. The case arose during the War of 1812 when the owners of a merchant ship sought to recover the profits they lost when

95 SEDGWICK 1847 at 2-3.
96 See McGrane Cox, Chancellor Kent at Yale (Part II), 17 YALE L.J. 553, 562 (1908) (quoting Story’s dedication of his treatise on conflict of law to Kent: “You have done for America what Mr. Justice Blackstone in his invaluable commentaries has done for England.”)
97 See 2 JAMES KENT, COMMENTARIES ON AMERICAN LAW vii-ix (6th ed. 1848).
99 See KENT, supra note 97, at 480 n.a.
100 See id. on this Kent notes that Sedgwick had criticized Kent’s earlier edition for having overlooked this distinction. Kent relies that: “These commentaries are not calculated to embody all of the nice, or arbitrary, or fanciful distinctions that are to be met in the reports. I do not regard the distinction alluded to as well founded or supported.” Id. In this, Kent seems not to be guilty of the ultra-narrow rules and slavish adherence to precedent of which he has been accused.
a privateer improperly delayed their vessel. Story, who in addition to being an Associate Justice of the United States Supreme Court, was the most respected legal scholar of the time, heard the case when he was riding circuit. The opinion he wrote was, like many of his opinions, eloquent and full of common sense. After reviewing the applicable case law and finding no authority awarding lost profits in similar situations, he went on to say:

Independent however of all authority, I am satisfied upon principle, that an allowance of damages upon the basis of a calculation of profits is inadmissible. The rule would be in the highest degree unfavorable to the interests of the community. The subject would be utter uncertainty. The calculation would proceed upon contingencies, and would require a knowledge of foreign markets, to an exactness in point of time and value and would sometimes present embarrassing obstacles. Much would depend upon the length of the voyage, and the season of arrival, much upon the vigilance and activity of the master, and much upon momentary demand. After all, it would be a calculation upon conjecture, and not upon facts.

Other courts shared their reluctance to award damages. They based their refusal to award lost profits on two forms of analysis, sometimes using one, sometimes using the other, and sometimes using both. One form of analysis simply carried on Justice Story’s argument made in *The Lively* and looked at the facts of the particular case to hold that the uncertainties inherent in the venture meant that any profits that would be made were purely speculative. The other analysis stemmed from the previously-described jurisprudence of the time that attempted to find a mechanical formula to govern every case so that the element of human judgment would be removed completely from the calculation of damages. Courts applying this form of analysis (if that term may be applied to this mechanical jurisprudence) combed the precedents, looking for a rule that would govern the damages calculation. None of these rules allowed the court to do what a modern court would do and simply look at how much better off the plaintiff would have been if the defendant had fulfilled its legal obligations.

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103 See id. at 632.
106 15 Fed. Cas. at 633.
107 See, e.g., Jones v. Van Patten, 3 Ind. 109, 112 (Ind. 1851) (reversing award profits lost on flatboat trip down Mississippi River and stating that reliance damages should have been awarded instead). See also Larabee Flour Mills Co. v. Mo. Pac. Rwy. Co., 116 P. 901, 903 (Kan. 1911) (referring to “[t]he old idea that profits were never recoverable”).
108 See supra, text accompanying notes 83-88.
109 See, e.g., Blanchard v. Ely, 21 Wend. 342, 345 (N.Y. 1839) (court in case involving building of boat sought other boat-building cases).
110 *Cf.* *RESTATEMENT (SECOND) CONTRACTS* § 347 (1989) (damages measured by injured party’s expectation interest).
Justice Story himself combined the two bases for denying lost profits in another privateering opinion, *The Amiable Nancy*:\[111\]

The probable or possible benefits of a voyage, as yet in fieri, can never afford a safe rule by which to estimate damages in cases of marine trespass. There is so much uncertainty in the rule itself, so many contingencies which may vary or extinguish its application, and so many difficulties in sustaining its legal correctness, that the court cannot believe it proper to entertain it. In several cases in this courts, the claim for profits has been expressly overruled; and in Del Col v. Arnold, (3 Dall 333.) and the Anna Maria, (2 Wheat. Rep. 327.) it was, after strict consideration, held that the prime cost or value of the property lost, at the time of loss, and in the case of injury, the diminution in value, by reason of the injury, with interest upon such valuation, afforded the true measure for assessing damages. The rule may not secure complete indemnity for all possible injuries; but it has certainty and general applicability to recommend it, and in almost all cases, will give a fair and just recompense.\[112\]

Sedgwick discussed the tendency toward narrow rules with mechanical formulas in his 1847 treatise on damages,\[113\] a treatise that became a classic and went through nine editions over the next 73 years.\[114\] Sedgwick complained about the narrow precise damage rules of American law\[115\] and quoted a passage in which Justice Story compared treatises on the common law their civil law counterparts, saying that the former “contain little more than a collection of the principles laid down in the adjudged cases, with scarcely an attempt to illustrate them by any general reasoning” while the civilians “discuss every subject with an elaborate theoretical fullness and accuracy, and ascend to the elementary principles of each particular branch of the science.”\[116\]

In fact, one can get an idea of the way the law of damages evolved simply by studying the table of contents of Sedgwick’s treatise as it went through its many editions. In the 1847 edition, there are entire chapters devoted to rules for particular types of transactions these include chapters titled “Rule of Damages in Actions Brought for Breach of Real Covenants,” “The Measure of Damages in Actions Growing Out of the Contracts of Principal and Surety,” “Rule of Damages as Between Principal and Agent,” and “The Rule of Damages in the Action of Trover.”\[117\] There is a chapter containing

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16 U.S. 546 (1818).
112 *Id.* at 561.
113 *Sedgwick, supra* note 76, at 2-3.
115 *Sedgwick, supra* note 76, at 2-3.
116 *Id.*, at 5 n.* (quoting Joseph Story, *Pref to Com. on Bailments*).
117 See *Sedgwick, supra* note 76, at ix-xiii.
general rule for tort damages, but it takes up only 9 pages of this 600-page work. The general rules for contract damages get slightly better treatment, being given 30 pages.

In contrast, the eighth edition of the same work, published in 1891, looks more like a modern work on the subject, organizing its discussion not on rules in particular types of cases but on broad general principles. It begins with a “General View of the Subject,” which contains, among other things, a history of Anglo-American damages law and a summary of the damages rules of other legal systems. It then devotes an 88-page chapter to a discussion of general principles of compensation in damages jurisprudence. An 89-page chapter on Consequential Damages is followed by a chapter on Certain and Uncertain Damages (i.e., the rule that damages must be proven with reasonable certainty). There are also chapters on Avoidable Consequences, The Measure and Elements of Value, Exemplary Damages, Liquidated Damages and other topics, most of which would be of interest to modern readers.

But in the jurisprudence of the early nineteenth century, there was no room for general rules about lost profits. In fact there was little room for the general rule that damages should be whatever makes the plaintiff whole. Instead, there was a myriad of narrow rules. If profits were lost because the defendant breached its contract to sell goods, the plaintiff’s recovery was via the rule for the sale of goods. If the plaintiff lost profits because the defendant breached a lease, the recovery was determined by the rules for breach of leases.

III.  **BLANCHARD v. ELY – THE CASE THAT ANTICIPATED HADLEY v. BAXENDALE**

In 1839, New York’s Supreme Court of Judicature, then the state’s highest court, used a new theory to deny recovery of lost profits. *Blanchard v. Ely* was a suit to recover the unpaid balance of the $12,500 price to be paid for the building of a steamboat to ply the Susquehanna River between Oswego and Wilkes-Barre. The defendants claimed offsets because the boat the defendants delivered had defects that not only required repairs, but also required that the defendants cancel planned trips, causing them

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118 See id.
119 See id.
121 See id. ch. I.
122 See id. ch. II.
123 See id. ch. IV. (Chapter III is devoted situations when only nominal damages are awarded).
124 See id. ch. V.
125 See id. ch. VI.
126 See id. ch. VIII.
127 See id. ch. XI.
128 See id. ch. XII.
129 See, e.g., id ch. VII (expenses of litigation).
130 21 Wend. 342 (N.Y. 1839).
131 See id. at 342-43.
in turn to lose profits of $100 per trip. The trial judge instructed the jury that they were should deduct from the unpaid price the cost of repairing the defects, but not the lost profits. Addressing the propriety of this instruction, Justice Cowen, writing for the Supreme Court, said:

No common law authority was cited at the bar, one way or the other, having any direct application to the measure of damages in such a case as this; nor am I aware that any exists. If there be none, it is somewhat singular, considering the many contracts for building boats and other vessels which must have been made in England and this country.

While it strikes the modern reader as strange that the court would not ask whether lost profits were generally recoverable, but would instead look for a case of lost profits in a boat-building contract, this search for a narrow rule based on the type of transaction involved was still the norm in 1839.

Finding no boat-building cases, the court did go further afield and looked at cases involving breach of warranty in the sale of real estate. There, the court cited one of its earlier opinions that in turn echoed the reasoning of Justice Story in *The Lively*: “it would be ruinous and oppressive to make the seller respond in damages, for any accidental rise in the value of the land or increased value in consequence of the improvements made by the purchaser.” The court then went on to quote still another of its own opinions, saying that “[t]he safest rule is, to limit the recovery, as much as possible, to an indemnity for the actual injury sustained, without regard to the profits the plaintiff has failed to make.” After discussing similar analogous rules with respect to sales of chattels, the opinion proceeded to break with tradition and consider a rule of general application:

In short, it will be seen by the cases cited and many more, that on the subject in question, courts are more and more falling into the track of the civil law, the rule of which is laid down by a learned writer: “In general, the parties are deemed to have contemplated only the damages and interest which the creditor might suffer from the non-performance of the obligation, in respect to the particular thing which is the object of it; and not such as may have been accidentally occasioned thereby in respect to his own affairs[,]” 1 Evans, Poth., 91 Lond. ed. 1806. He illustrates this rule by a rise of value in goods which the promisor fails to deliver. He adds, if the lessor’s title to a house fail, he is bound to pay his lessee the expense of removal, and indemnify him against the advance of rents, but not against the loss of custom in a business he may have established while

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132 See id. at 343.
133 See id. at 344.
134 In his *the Common Law Tradition*, Karl Llewellyn lauds Cowen as one of the masters of what Llewellyn called the “Grand Style” of opinion writing. See LLEWELLYN, supra note 101, at 64-68, 423-26.
135 21 Wend. at 345.
136 Id. at 346 (quoting Dimmick v. Lockwood, 10 Wend. 150 (N.Y. 1833)).
137 Id. (quoting Baldwin v. Munn, 2 Wend. 399, 406 (N.Y. 1829)).
residing in the house. He also adverts to the distinction that the vendor may, notwithstanding, incur liability of extrinsic damages of the creditor, if it appear they were stipulated for or tacitly submitted to in the contract. One instance of this is that of stipulating to deliver a horse in such time that a certain advantage may be gained reaching such a place. There, the debtor, on default, pay for the loss of the advantage.\textsuperscript{138}

This is not only the reasoning of \textit{Hadley v. Baxendale},\textsuperscript{139} articulated fifteen years before the Court of the Exchequer’s opinion in \textit{Hadley},\textsuperscript{140} but it is the same authority (William Evans’s translation of Pothier’s \textit{Traité des obligations}) that Baron Parke so forcefully put forward early in the oral arguments in \textit{Hadley}.\textsuperscript{141} If things had gone differently, \textit{Blanchard v. Ely} might be the opinion that everyone reads in their first-year contracts course, but, as we shall see, later events conspired to make \textit{Blanchard} a little-known footnote in the law of damages.

\textbf{IV. \textit{MASTERTON v. BROOKLYN ALLOWS LOST PROFITS IN LIMITED CIRCUMSTANCES}}

In 1845, everything changed. In an opinion that is little remembered today, the New York high court unequivocally announced that lost profits could be awarded in a breach of contract case. \textit{Masterton v. Brooklyn}\textsuperscript{142} was a suit by a firm that had contracted to supply the marble to be used in the new city hall in Brooklyn. The city had run out of funds and ceased construction when it had taken delivery of only a small fraction of the

\begin{footnotesize}
\begin{enumerate}
\item\textsuperscript{138} Id at 348.
\item\textsuperscript{139} 15 Ex. 341 (1854).
\item\textsuperscript{140} The Supreme Judicial court of Maine articulated the same rule even earlier, saying:  

\begin{quote}
In general [in cases of breach of contract], the delinquent party is holden to make good the loss occasioned by his delinquency. But his liability is limited to direct damages, which, according to the nature of the subject, may be contemplated or presumed to result from his failure. Remote or speculative damages, although susceptible of proof, and deductible from the nonperformance, are not allowed.
\end{quote}

\begin{footnotesize}
Miller v. Mariner’s Church, 7 Me. 51, 55 (Me. 1830). The case has rather picturesque facts. The plaintiff was the warden of the state prison. He brought the action against the trustees of a church for the price of hammered stone (presumably rocks broken by the convicts) delivered for use in a new church building. The trustees counterclaimed for damages for late delivery and defects in workmanship. See id. at 51.

Later courts (including the United States Supreme Court) frequently cited the opinion, not for the \textit{Hadley} rule, but for the rule that a plaintiff may not recover damages that could have been avoided without undue burden. See, e.g., Pullman’s Palace Car Co. v. Metropolitan Street Rwy. Co., 157 U.S. 94, 111 (1895).
\item\textsuperscript{141} See 156 Eng. Rep. at 147-48.
\item\textsuperscript{142} It’s not the same passage that Parke said stated the “sensible rule”. \textit{Id.} at 147. The passage quoted by the \textit{Blanchard} court is actually a more restrictive form of the rule, requiring not only that the potential loss be foreseeable, but that the circumstances be such that the party such that the defendant can be thought to have consciously assumed the risk. This rule, now referred to as the tacit agreement test, is still applied in New York (see infra, Part VI. C.) even though most other Anglo-American jurisdictions only require the loss be foreseeable.
\end{footnotesize}
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\end{footnotesize}
marble. The sellers sued, the trial judge, who was the son of Chancellor James Kent, the author of *Kent’s Commentaries*, charged the jury that they should award as damages the difference between the contract price and what it would have cost the plaintiffs to acquire, process, and deliver the marble. The defendants objected to the charge and requested a charge that no profits could be awarded. When Judge Kent refused their request, the defendants appealed. The Supreme Court of Judicature reversed the trial judge and granted a new trial, but not because he instructed the jury to award lost profits. His error, they said, was instructing the jury to take into account in their damage calculations the subcontract the plaintiffs had made in order to acquire the marble.

In his opinion, Chief Justice Nelson acknowledged that “[i]t is not to be denied that there are profits or gains derivable from a contract which are uniformly rejected as too contingent and speculative in their nature, and too dependent upon fluctuation of markets and the chances of business, to enter into a safe or reasonable estimate of damages.” He also noted that the civil law generally denied recovery of lost profits, but for a different reason. Again quoting from Evan’s translation of Pothier, the chief justice explained that the civil law denied lost profits because of what would become known in the common law world as “the rule of *Hadley v. Baxendale*:”

“In general,” says Pothier, “the parties are deemed to have contemplated only the damages and interest which the creditor might suffer from the non-performance of the obligation, in respect to the particular thing which is the object of it, and not such as may have been incidentally occasioned thereby in respect to his other affairs.”

In other words, lost profits are not disallowed because of a general rule prohibiting their recovery, but because they are not contemplated at the time of contract formation. The chief justice noted that this objection to the recovery of lost profits did not apply in the case where the damages sought were “the direct and immediate fruits of the contract entered into between the parties.”

With respect to the argument that the profits were too uncertain to be awarded as damages, the chief justice said the concern that it was impossible to predict the way that

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143 *See id.* at 64-65.
144 *See id.* at 66.
145 *See id.*
146 *See 7 Hill* at 72-74.
147 The Supreme Court of Judicature issued three opinions in the case. That of Chief Justice Nelson is appears first in the report and is the longest.
148 7 Hill at 67.
149 *Id.* at 68.
150 We use the word “contemplated” rather than foreseeable, because that was the term more commonly used prior to the mid-twentieth century. The meaning of that term has changed over the years and for many years it meant that the damages had to be not only foreseeable, but actually foreseen and in some jurisdictions the defendant had to accept liability, at least tacitly. *See infra* text accompanying notes Part VI. C.
151 *See 7 Hill* at 69.
costs would change over the life of the contract, the sort of concern that had troubled Justice Story.\textsuperscript{152} could be dealt with by estimating the plaintiff’s cost of fulfilling the contract on the market prices prevailing at the time of breach.\textsuperscript{153} From the unpaid contract price would be subtracted the costs the plaintiff did not incur because it did not have to continue performance. Rather than trying to estimate how the costs of labor and materials would rise or fall over the three and a half years remaining in the contract, the jury should estimate the damages on the basis of the prices prevailing at the time of the breach.\textsuperscript{154} The chief justice used the reasoning that would later form the basis for the \textit{Hadley v. Baxendale} opinion to hold that the jury should not take into account the subcontracts the plaintiffs had entered into to acquire the unfinished marble. He said that the defendants had no control over the making of the subcontracts and therefore were neither required to assume the burden of unfavorable subcontracts nor to gains the benefits from favorable ones.\textsuperscript{155} In other words, it was not contemplated at the time the prime contract was made that the plaintiff would enter into subcontracts that deviated from the norm for that kind of contract.

The chief justice did not give the jury free rein to award damages as they thought fit. In fact, he gave what could be a good summary of the modern rule that lost profits can be recovered only when their amount is proven with reasonable certainty:

\begin{quote}
[T]he parties will be obliged to go into an inquiry as to the actual cost of furnishing the article at the place of delivery; and the court and jury should see that in estimating this amount it be made upon a substantial basis and not left to rest upon the loose and speculative opinions of witnesses. The constituent elements of the cost should be ascertained from sound and reliable sources; from practical men, having experience in the particular department of labor to which the contract relates. It is a very easy matter to figure out large profits on paper; but it will be found that these, in a great majority of the cases, become seriously reduced when subjected to the contingencies and hazards incident to actual performance. . . . [A jury] should not overlook the risks and contingencies which are almost inseparable from the execution of contracts like the one in question, and which increase the expense independently of the outlays in labor and capital.\textsuperscript{156}
\end{quote}

In a separate opinion, Justice Beardsley concurred with proposition that lost profits could be recovered when they were direct damages but made it clear that they could not be recovered in contract when they were consequential damages:

Remote and contingent damages, depending on the result of successive schemes or investments, are never allowed for the violation of

\begin{footnotes}
\item[152] See supra, text accompanying notes 102-06.
\item[153] See 7 Hill at 70.
\item[154] See id. at 71.
\item[155] See id. at 72.
\item[156] Id. at 72-73.
\end{footnotes}
any contract. But profits to be earned and made by the faithful execution of a fair contract are not of this description. A right to damages equivalent to such profits results directly and immediately from the act of a party who prevents the contract from being performed.\textsuperscript{157}

Other courts soon followed \textit{Masterton} and allowed plaintiffs to recover lost profits in contract cases as long as they were direct damages.\textsuperscript{158} In \textit{Fox v. Harding},\textsuperscript{159} itself a widely cited opinion, the Supreme Court of Massachusetts said that lost profits could be recovered if they were “the direct and immediate results” of the contract, but not if they were the result of “independent and collateral undertakings.”\textsuperscript{160}

As noted above, the first edition of Sedgwick’s treatise on damages was published in 1847, shortly after the \textit{Masterton} opinion appeared. And in addition to all of the chapters dealing with the narrow rules in individual types of actions, Sedgwick did have a chapter titled “Of Remote and Consequential Damages.” In this chapter, he stated the general rule as to consequential damages—they are not awarded except in the case of deliberate wrongdoing:

\begin{quote}
[T]he law refuses to take into consideration any damages remotely or consequentially resulting from the act complained of. This general principle pervades the civil law as well as the common law, and applies equally to cases of breach of contract, and of violation of duty; to all cases, in short, where no complaint is made of a deliberate intention to injure. In these latter cases we have seen that our law does not pause at the line of mere compensation, but proceeds to punish the offender.\textsuperscript{161}
\end{quote}

But he went on to say that this rule and the reasons given for it “are far from being uniform.” He took the position that in actuality the rule against the award of consequential damages was simply a generalization from what we today refer to as “the rule of \textit{Hadley v. Baxendale}.” In a passage that Hadley’s barristers were to quote in their argument before the Court of the Exchequer, Sedgwick said:

\begin{quote}
It is sometimes said in regard to contracts, that the defendant shall be held liable for those damages which both parties may fairly be supposed to have at the time contemplated as likely to result from the nature of the
\end{quote}

\begin{footnotes}
\item[157] Id. at 74.
\item[158] See, e.g., Chicago & Rock Island R.R. Co v. Ward, 16 Ill. 522, 530-31 (1855) (farmer could recover lost profits where railroad breached covenant to maintain fence); Bridges v. Stickney, 38 Me. 361, 368 (1854) (allowing recovery of direct damages but not consequential damages); Hoy v. Gronoble, 34 Pa. 9, 10-11 (1859) (sharecropper could recover profits lost when landowner breached oral contract); Hinckley v. Beckwith, 13 Wis. 31, 35 (1860) (profits of sawmill recoverable).
\item[159] 61 Mass. (7 Cush.) 516 (1851).
\item[160] Id. at 522.
\item[161] SEDGWICK, supra note 76, at 63-64.
\end{footnotes}
agreement, and this appears to be the rule adopted by the writers on the civil law.\textsuperscript{162}

Sedgwick then went on to give a picturesque example from the ubiquitous Pothier. If a seller breaches a contract to sell a horse, the damages are the difference between the contract price and the price the buyer has to pay to obtain a substitute animal.\textsuperscript{163}

But, on the other hand, if the purchaser were a canon, and by reason of the non-delivery of the horse could not arrive at his residence in season to receive his \textit{gros fruits}, the seller is not liable for the loss of those \textit{gros fruits} because this was not foreseen at the time of the contract.\textsuperscript{164}

After another example, Sedgwick noted that Pothier had further qualified his initial qualification, saying:

\begin{quote}
But if on the other hand, the horse above referred to had been sold for the express object of enabling the canon to arrive in time for his \textit{gros fruits}, . . . then the injuries which otherwise would be remote and consequential, become direct and immediate, and constitute a valid claim, as forming part of the contract between the parties.\textsuperscript{165}
\end{quote}

This statement goes beyond the rule of \textit{Masterton} because it deals with damages that are not the failure to receive the other party’s performance as in \textit{Masterton}, but are what we today would likely call a consequential loss. It’s a little confusing to the modern reader because it makes a distinction between direct damages and consequential damages that is different from one we make. We generally think of direct damages as those that compensate the injured party for the loss the promised performance, whereas consequential damages compensate for additional losses, such as the loss of profits on contracts with third parties.\textsuperscript{166} We say that these consequential losses are recoverable in contract only if they were foreseeable the breaching party at the time they entered into the contract.\textsuperscript{167} Under the Pothier/Sedgwick terminology, consequential damages are those damages that were not foreseeable and thus were never recoverable, absent deliberate wrongdoing. Losses that were within the contemplation of the parties at the time they entered into the contract were called direct damages, even if they were were the result of some collateral undertaking, such as a contract to resell the purchased goods.

V. \textit{GRiffin v. COLVER COMPLETES THE TRANSFORMATION}

\textsuperscript{162} \textsc{Sedgwick}, \textit{supra} note 76, at 64 quoted at \textit{Hadley}, 156 Eng. Rep. at 147, 9 Ex. at 45 (argument of Keating and Dowdeswell).

\textsuperscript{163} This is of course the modern rule. \textit{See} UCC \S\ 2-713. Actually, the example seems to assume that the contract was made at the market price because it speaks in terms of a rise in prices necessitating the payment of a higher price.

\textsuperscript{164} \textsc{Sedgwick}, \textit{supra} note 76, at 64.

\textsuperscript{165} \textit{Id.} at 65.

\textsuperscript{166} \textit{See, e.g.}, Schonfeld v. Hilliard, 218 F.3d 164, 175-76 (2d Cir. 2000).

\textsuperscript{167} \textit{See, e.g.}, \textsc{Restatement (Second) of Contracts} \S\ 351 (1989).
In 1854, the Court of the Exchequer issued its famous opinion in *Hadley v. Baxendale*. The opinion quickly became known in the United States, but it didn’t have much immediate effect on the recovery of lost profits. There were two reasons for this. First, the rule was already known in the United States, so much so that Kent had years before set out a version of it in his *Commentaries*. More importantly, American courts had not yet begun awarding lost profits as damages, except where they were direct benefit of the bargain damages.

Four years later, however, American courts did begin awarding lost profits as consequential damages. In 1858, the newly-established New York Court of Appeals issued its opinion in *Griffin v. Colver*. Substantively, the facts of *Griffin* were identical to those of *Blanchard v. Ely*, and arguably *Griffin* should not even have been appealed. The case involved the building, not of a steamboat, but of a steam engine for a lumber mill. Once again, the builder sued for the contract price, and once again the defendant attempted to offset the profits lost because the product was not delivered on time. The referee before whom the case was tried held that the lost profits were not a proper measure of damages. Instead, he awarded the defendants $66.12 as compensation for the loss of use of their property.

This was in keeping with a rule of the time that the proper measure of damages in such cases was the use value of the property or capital involved. After the supreme court affirmed the judgment entered on the referee’s report, the plaintiff appealed to the new Court of Appeals.

The Court of Appeals’ opinion gets directly to the point. It begins by acknowledging that there is a “rule which precludes the allowance of profits, by way of damages, for the breach of an executory contract.” But it then immediately states that the rule is not to be taken literally:

To determine whether this rule was correctly applied by the referee, it is necessary to refer to the reason upon which it is founded. It is not a primary rule, but is a mere deduction from that more general and fundamental rule which requires that the damages claimed should in all cases be shown, by clear and satisfactory evidence, to have been actually sustained. It is a well established rule of the common law that the damages to be recovered for a breach of contract must be shown with certainty, and not left to speculation or conjecture; and it is under this rule

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Kent phrased it this way: “Damages for breach of contract are only those which are incidental to and directly caused by the breach and may be supposed to have been in the contemplation of the parties, and not speculative profits or accidental or consequential losses.” *Id.*

Later commentators may have failed to understand the significance of Kent’s statement because they did not realize that when Kent wrote, the term “consequential damages” was understood to exclude any damages that were contemplated by the parties at the time they entered into the contract.

169 16 N.Y. 489 (N.Y. 1858).


171 See *id.* at 588

172 See infra Part VI.B.

173 See 22 Barb. at 593.

174 16 N.Y. at 491.
that profits are excluded from the estimate of damages in such cases, and not because there is anything in their nature which should \textit{per se} prevent their allowance. Profits which would certainly have been realized but for the defendant’s default are recoverable; those which are speculative or contingent are not.\footnote{Id. at 491.}

This one paragraph has become the basis for the modern law of lost profits: Lost profits may be recovered in contract, but only if they are proven with certainty. (We now say “reasonable certainty.” This will be discussed later.\footnote{See infra, text accompanying notes 256-64.})

This was a huge change from the prior law. Even after \textit{Masterton}, courts had uniformly refused to award lost profits as consequential damages in contract cases. While some courts had used the difficulty of proof as a justification for the rule that lost profits could not be recovered as consequential damages, they nevertheless adhered to it as a \textit{per se} rule, rather than considering the possibility that in some cases the lost profits could easily be determined.\footnote{See, e.g., Taylor v. Maguire, 12 Mo. 313, 319-20 (Mo. 1848). Interestingly, another justification the court gave for denying the recovery of lost profits was that “[t]he loss . . . which forms the criterion of damages . . . must be a loss within the probable contemplation of the parties at the time of the execution of the contract.” \textit{Id.} at 318. This is just one more instance of American courts anticipating the \textit{Hadley} rule.}

To support the novel proposition it was advancing as settled law, the court used a technique that would later be perfected by Judges such Benjamin Cardozo on this same New York Court of Appeals and Roger Traynor on the California Supreme Court. It analyzed the leading cases that seemed to support the contrary point of view and argued that if you looked at the facts and what the court actually decided on the basis of those facts, rather than looking at the language these courts used in support of their reasoning, the cases really did support the judge’s rule, not the opposing rule for which they were cited.\footnote{See Arthur L. Corbin, \textit{Mr. Justice Cardozo and the Law of Contracts}, 39 COLUM. L. REV. 56 (1939) (discussing Cardozo’s method); Pac. Gas & Elect. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641 (Cal. 1968) (example of Traynor’s method). \textit{Cf.} Grant Gilmore, \textit{Legal Realism: Its Cause and Cure}, 70 Yale L.J. 1037, 1045 (1961) (alternative description of Cardozo’s method).} More importantly, it embraced the emerging trend toward replacing narrow, situation-specific rules with broad principles of general application.\footnote{See GRANT GILMORE, AGES OF AMERICAN LAW 41-67 (1977).}

To work this transformation, the court began by discussing a group of rules that depend on the market price of goods and attempting to show that these are in reality specific applications of the general rule that lost profits can be recovered when they can be proven with certainty and cannot be recovered when the cannot.\footnote{See 16 N.Y. at 491-92.} It cited the rule that in an action for breach of a contract to transport goods, the damages are the difference between the price of the goods at the point of origin and the price at the destination and the rule that where a seller breaches a contract to sell goods, the damages are the difference between the contract price and the market price at the time and place.
for delivery. “[T]his,” the court said, “amounts to an allowance of profits.” \(^{181}\) It is recoverable because “those profits do not depend on a contingency.” \(^{182}\) The court then goes on to distinguish the cases that do not allow the recovery of profits in the case of the illegal capture of goods at sea or in the case of insurance for goods lost at sea. In those cases, “the fluctuation of markets and the contingencies affecting the length of the voyage render every calculation of profits speculative and unsafe," \(^{183}\) whereas in cases involving the transportation of goods by land, the market price at the destination “can be ascertained with reasonable certainty.” \(^{184}\)

One can certainly question this reasoning. The rules cited are not rules allowing the injured party to recover its lost profits. They are rules that give a fixed measure of damages that will in many cases approximate the party’s actual lost profits. But they if they were really intended to give the injured party its lost profits, they would, like their modern equivalents, allow the injured party to prove that its damages were greater than the amount allowed by the rule (or to allow the defendant to prove that the damages were less). For instance, there might be cases where the buyer or the shipper had a contract to sell the goods to a third party at a price above (or below) the prevailing market price (perhaps because the contract had been made at a time when price was higher or lower) or there might be cases where the buyer or the shipper needed the goods for a special purpose (think of Hadley’s mill shaft). The pre-Griffin rules made no provision for that. \(^{185}\)

As further support for the idea that it was the difficulty of determining the profits to be made from a sea voyage that was the reason for the per se rule against allowing such profits, the court quoted part of the passage from Justice Story’s opinion in The Lively quoted earlier in this article. \(^{186}\)

Next, the court jumped to a truly amazing conclusion: “Indeed, it is clear that whenever profits are rejected as an item of damages, it is because they are subject to too many contingencies, and too dependent upon the fluctuations of markets and the chances

\(^{181}\) Masterton, 16 N.Y. at 491.
\(^{182}\) Id.
\(^{183}\) Id. at 492.
\(^{184}\) Id.
\(^{185}\) See supra, text accompanying notes 105-34.
\(^{186}\) The opinion said:

[T]hat these are the true reason is shown by the language of Mr. Justice Story in the Schooner Lively (1 Gall. 315) which was a case of illegal capture. He says: “Independent, however, of all authority, I am satisfied upon principle, that an allowance of damages upon the basis of a calculation of profits is inadmissible. The rule would be in the highest degree unfavorable to the interests of the community. The subject would be utter uncertainty. The calculation would proceed upon contingencies, and would require a knowledge of foreign markets, to an exactness in point of time and value and would sometimes present embarrassing obstacles. Much would depend upon the length of the voyage, and the season of arrival, much upon the vigilance and activity of the master, and much upon momentary demand. After all, it would be a calculation upon conjecture, and not upon facts.
of business, to constitute a safe criterion for an estimate of damages.” 187 We have added the emphasis to make clear how incredibly broad a statement the court was making. It is particularly significant, because cases in New York and other American jurisdictions had almost never allowed the recovery of lost profits as consequential damages and had given many reasons for not doing so, most commonly that there was a rule that mandated a specific damages formula that did not include lost profits. 188 But the court goes on to say: “The decision in the case of Blanchard v. Ely (21 Wend., 342) must have proceeded on this ground and can be supported on no other.” 189 The court explains that the “Rule of Pothier” (i.e., the rule now known as the Rule of Hadley v. Baxendale) as it was discussed in Blanchard v. Ely and says that it cannot have applied in that case:

In Blanchard v. Ely the damages claimed consisted in the loss of use of the very article which the plaintiff had agreed to construct; and were, therefore in the plainest sense the direct and proximate result of the breach alleged. Moreover, that use was contemplated by the parties in entering into the contract, and constituted the object for which the steamboat was built. It is clear, therefore, that the rule of Pothier had nothing to do with the case. Those damages must then have been disallowed, because the consisted of profits depending, not, as in the case of a contract to transport goods, upon a mere question of market value, but upon the fluctuations of travel and of trade, and many other contingencies. 190

This reasoning is interesting for a couple of reasons. First, contrary to the court’s assertion, it is not at all clear that the civil law consequential damages rule (the “rule of Pothier”) had nothing to do with the case. It might well have precluded recovery in Blanchard v. Ely. It is true that the rule of Hadley v. Baxendale, as it is now applied in most American jurisdictions, would hold that the builder’s knowledge the boat was to be used to carry passengers for hire would be enough to make the builder liable for the normal profits lost on account of delays in making it serviceable. 191 But the civil law rule, at least as understood by the Blanchard v. Ely court, required more than mere foreseeability. In a portion of the opinion previously quoted, the Blanchard court had said:

[Pothier] also adverts to the distinction that the vendor may, notwithstanding, incur liability of extrinsic damages of the creditor, if it appear they were stipulated for or tacitly submitted to in the contract. On instance of this is that of stipulating to deliver a horse in such time that a certain advantage may be gained reaching such a place. There, the debtor, on default, pay for the loss of the advantage. 192

187 Masterton, 16 N.Y. at 492 (emphasis supplied).
188 See supra, text accompanying notes 108-37.
189 Masterton, 16 N.Y. at 492.
190 Id. at 494.
191 See, e.g., RESTATEMENT (SECOND) CONTRACTS § 351, ill. 5 (1989).
192 21 Wend. at 348 (emphasis supplied).
This seems to say that in order to recover consequential damages, the plaintiff must do more than simply show the defendant had reason to know the damages would be incurred; it must show the defendant had agreed, at least tacitly, that it would be liable for those damages. This rule, sometimes called the “tacit agreement test,” was adopted by most American jurisdictions in the years following Hadley v. Baxendale. Most American jurisdictions dropped it in favor of a more liberal reading of Hadley early in the twentieth century, but, interestingly, the courts of New York still retain it.

With Griffin’s rejection of the foreseeability requirement as the rule of decision in Blanchard v. Ely, that opinion became just another forgotten nineteenth century opinion. It was not cited in scholarly writing until 2005 when scholars writing about Hadley v. Baxendale in honor the 150th anniversary of the issuance of that opinion noted that an American court had adopted the same rule a decade and a half before the Court of the Exchequer.

VI. LATER DEVELOPMENTS

A. The Griffin Rule Spreads

If Blanchard was quickly forgotten, Griffin quickly gained notoriety. It soon became known as the “leading case” on the recovery of lost profits. Courts in other jurisdictions began almost immediately to cite it for the proposition that lost profits were now a recoverable item of damages.

The first of these was the Wisconsin Supreme Court in Hinkley v. Beckwith, decided just two years after Griffin. A sawmill lease provided that the lessors would make any repairs that cost more than five dollars and were necessary to keep the sawmill running. When the engine failed in the last sixty days of the lease term, they refused to repair it. In the resulting lawsuit, the trial court awarded the lessees the profits they had lost in during the time the mill was out of service and the defendant appealed. Interestingly, both parties cited Griffin in their briefs to the Wisconsin Supreme Court. The lessees cited it for the proposition that lost profits were recoverable and the lessors

193 See infra, Part VI. C.
196 See, e.g, Jones, v. Nathop, 1 P. 435, 437 (Colo. 1883) (describing Griffin as “the leading American case”); Western Gravel Road Co. v. Cox, 39 Ind. 260 (Ind. 1872) (Griffin said to be leading American case on lost profits).
197 See also Manville v. Western Union Tel. Co., 37 Iowa 214, 219 (1873) (calling Griffin “a leading American authority on the subject”).
198 13 Wis. 31 (Wisc. 1860).
199 See id. at 33.
200 See id. at 32.
cited it for the proposition that they were not.\textsuperscript{201} The supreme court sided with the lessees, discussing \textit{Griffin} at length and saying the it “fully sustains” the rule allowing lost profits to be recovered.\textsuperscript{202}

After \textit{Hinckley}, the \textit{Griffin} rule spread by stealth. Courts in many jurisdictions issued opinions upholding denials of lost profits (or reversing awards of lost profits), but in doing so they cited \textit{Griffin}, saying that under proper circumstances lost profits were recoverable. It was just that these were not the proper circumstances.\textsuperscript{203} The most important of these opinions was that of the United States Supreme Court in \textit{United States v. Behan}.\textsuperscript{204} Behan had been working under a contract with the Army to make improvements in the harbor of New Orleans when the Army decided that it was not worthwhile to continue the work and terminated the contract.\textsuperscript{205} Behan thereupon petitioned the War Department for his expenses to date and the profit he would have made if he had been allowed to complete the contract.\textsuperscript{206} When he was not paid, he sued in the Court of Claims, which awarded him his expenditures but said that he had not proven his lost profits.\textsuperscript{207} The Supreme Court affirmed the Court of Claims, but in doing so it stated unequivocally that lost profits may be recovered in proper circumstances and said this was so well established that “[i]t is unnecessary to review the authorities on this subject.”\textsuperscript{208} \textit{Behan} added weight to the growing \textit{Griffin} consensus and by the end of the 1880s courts throughout the nation had acknowledged the principle that lost profits were a proper item of damages.\textsuperscript{209}

\textsuperscript{201} See id. at 31.
\textsuperscript{202} See id. at 34-35.
\textsuperscript{203} See, e.g., Jones. v. Nathop, 1 P. 435, 437 (Colo. 1883)(describing \textit{Griffin} as “the leading American case,” but rejecting lost profits claim because profits were “speculative”); Western Gravel Road Co. v. Cox, 39 Ind. 260 (Ind. 1872) (quoting \textit{Griffin} at length but holding that lost profits not proven with sufficient certainty); U.S. Tel. Co. v. Gildersleeve, 29 Md. 232, 250-51 (Md. 1868) (discussing \textit{Griffin} but reversing lost profit award because loss not foreseeable); Cushing v. Seymour, Sabin & Co., 15 N.W. 249, 250 (Minn. 1883)(citing \textit{Griffin} for proposition that lost profits can be recovered if reasonably certain but holding plaintiff’s lost profits not proven with reasonable certainty)
\textsuperscript{204} 110 U.S. 338 (1883).
\textsuperscript{205} See id. at 339-40.
\textsuperscript{206} See id. at 340-41.
\textsuperscript{207} See id. at 342-43.
\textsuperscript{208} See id. at 346.
\textsuperscript{209} See, e.g., Bell v. Reynold & Lee, 78 Ala. 511, 514 (1885); Jones. v. Nathop, 1 P. 435, 437 (Colo. 1883; Cohn v. Norton, 18 A. 595, 597 (Conn. 1889); Chicago R.R. Co. v. Hale, 83 Ill. 360 (1876); City of Terre Haute v. Hudnut, 13 N.E. 686 (Ind. 1887); Alexander v. Bishop, 13 N.W. 714, 717 (Iowa 1882); Stewart v. Power, 12 Kan. 596, 599-600 (1874); Cushing v. Seymour, Sabin & Co., 15 N.W. 249, 250 (Minn. 1883); Deming v. Grand Trunk R.R. Co. 48 N.H. 455, 471 (1869); Wisner v. Barber, 10 Ore. 342, 344 (1882) (“the allowance of profits is now well established”); McHose v. Fulmer, 73 Pa. 365, 873 (1873); Simmons v. Brown, 5 R.I. 299, 305-06 (R.I. 1858); Hinckley v. Beckwith, 13 Wis. 31 (Wis. 1860).

\textit{See also Ye Seng Co. v. Corbitt & Macleay}, 9 F. 423 (D. Ore. 1881) (relying on \textit{Griffin} to allow recovery of lost profits in admiralty for breach of charter-party); Shouse v. Neiswaanger, 18 Mo. App. 236, 251 (1885)(lost profits recoverable on remand if foreseeable).

\textit{See also cases cited in [immediately preceding note] By 1890, the Pennsylvania Supreme Court seems to have thought the recovery of lost profits in contract to be so uncontroversial that it found it unnecessary to cite a single authority in an opinion upholding a verdict for lost profits. Imperial Coal Co. v. Port Royal Coal Co., 20 A. 937, 937 (1890).}
Some the cases giving rise to these acknowledgments were the routine eighteenth century commercial cases (mills and shipping contracts continued to play leading roles)\textsuperscript{210} and some involved interesting situations. In 1889, the New Mexico Supreme Court relied on *Griffin* to allow a doctor to recover the fee he would have earned by travelling to a town a hundred miles away to treat a gunshot victim.\textsuperscript{211} A telegram asking him to come was not delivered in a timely manner, and as a result, the victim died before the doctor could treat him and earn his fee.\textsuperscript{212} The court said that under *Griffin*, the injured party is entitled to recover all damages, including gains prevented as well as losses sustained.\textsuperscript{213}

B. A New Rule Limiting Lost Profits

There were, however, still some bumps along the road to the present law of lost profits. One of these was created by the *Griffin* opinion itself. Like Ophelia (“the lady doth protest too much, methinks”)\textsuperscript{214}, Judge Selden knew he was on shaky ground when he tried to explain away *Blanchard v. Ely*, so he went on too long, and in doing so inadvertently created a new rule that slowed the development of the law of lost profits:

Had the defendants in the case of *Blanchard v. Ely* . . . taken the ground that the were entitled to recoup, not the uncertain and contingent profits of the trips lost, but such sum as they could have realized by chartering the boat for those trips, I think their claim must have been sustained. . . .

The rent of a mill or other similar property, the price which should be paid for the charter of a steamboat, or the use of machinery, &c., &c., are only susceptible of more exact and definite proof, but in a majority of cases would, I think, be found to be a more accurate measure of the damages actually sustained in the class of cases referred to . . . .\textsuperscript{215}

What the court is saying here is that if the lost profits are uncertain, the plaintiff can be awarded the lost profits of some other hypothetical enterprise that it could have entered into but for the defendant’s default. This led to courts adopting a number of narrow rules to be applied in similar situations. Most courts adopted some version of a rule that where a party is deprived of the use of property by the defendant’s action or omission, the measure of damages is not the profits lost, but the rental value of the property of which they were deprived. The reasoning by which they reached this conclusion varied. The Supreme Court of Iowa put it in terms of a *Hadley v. Baxendale* issue:

\textsuperscript{210} See, e.g., Pac. Sheet Metal Works v. Californian Canneries, Co., 164 F. 980, 985 (9th Cir. 1908) (lost profits awarded where storms delayed shipment); Morrow v. Mo. Pac. Rwy. Co., 123 S.W. 1034, 1039 (Mo. Ct. App. 1909) (involving delay in shipment of mill rolls);
\textsuperscript{211} Western Union Tel. Co. v. Longwill, 21 P. 339 (N.M. 1889).
\textsuperscript{212} See id. at 340.
\textsuperscript{213} See id. at 342.
\textsuperscript{215} 16 N.Y. at 496-97.
[O]n the principle that speculative profits are not deemed to have been within the contemplation of the parties, where there is some other more substantial basis on which to reckon the damages for breach of contract, it has been generally held that where the contract was for the completion of a building or boat, or for the use of land or machinery, or the like, the rental value of the use of which the party was deprived should be taken as the measure of his damage, and that he could not substitute therefor or include therein profits which he should have made in such use.\textsuperscript{216}

The court went on to say: “It is well established by the decided preponderance of authority that where future profits are in the contemplation of the parties, \textit{and there is no other basis on which damages for breach of contract can be estimated}, such profits may be made the basis for the recovery of damages.”\textsuperscript{217}

The Michigan Supreme Court, in a tort case where the defendant wrongfully took possession of the plaintiff’s boat, phrased the rule as a \textit{per se} rule disallowing profits and allowing the recovery of the rental value of the boat:

The measure of damages is not to be made to depend upon the use or non-use of the property by the defendant; neither can the use to which the plaintiff could have put the property during its detention, and the prospective estimates of profits therefrom, contingent upon his chance of business, determine the value of its use. Such rule would be too uncertain and speculative.”\textsuperscript{218}

The Illinois Supreme Court applied similar reasoning to reverse an award of lost profits and give a farmer the rental value of his land when the City of Chicago flooded the land and prevented him from growing a year’s crop.\textsuperscript{219} In doing so, it overruled a previous case allowing the farmer to recover his lost profits under similar circumstances.\textsuperscript{220}

Most courts, however, did not bother elaborating their reasoning, let alone qualifying the rule. They simply stated that the established rule was that the injured party was entitled to the rental value, not the lost profits.\textsuperscript{221} Ironically, \textit{Griffin} was often cited as the leading case for this rule.\textsuperscript{222}

\textsuperscript{216} Hichhorn, Mack & Co. v. Bradley, 90 N.W. 592, 595 (Iowa 1902).
\textsuperscript{217} Id. (emphasis supplied).
\textsuperscript{218} See also Connersville Wagon Co. v. McFarlan Carriage Co., 76 N.E. 294, 299 (Ind. 1905) (“the value of the used should be regarded as the basis for a recovery, where a case is made for an allowance of special damages growing out of a deprivation of the use of property”).
\textsuperscript{219} Aber v. Batton, 27 N.W. 564, 566 (Mich. 1886).
\textsuperscript{220} See City of Chicago v. Huenerbein, 85 Ill. 594, 595-96 (Ill. 1877).
\textsuperscript{221} See \textit{id}. at 596 (overruling Chicago & Rock Island R.R. Co v. Ward, 16 Ill. 522, 530-31 (1855).
\textsuperscript{222} See, e.g., Sinker, Davis & Co. v. Kidder, 24 N.E. 341, 341 (Ind. 1890) (relying on \textit{Griffin}); Benton v. Fay 64 Ill. 417, 420-21 (1872) (where operation of plant delayed because of late delivery of planning machine, damages were rental value of entire plant); Strobel Steel Const. Co. v. Sanitary Dist. Of Chicago,
Similarly, where sales agents for a sewing machine company sought the profits they lost because the company failed to supply the agents with machines as promised, the Iowa Supreme court, after an extensive discussion of Griffin, which it characterized as “regarded as a somewhat leading case,” held that the agents were entitled to the value of their time and that the trial court had erred in instructing the jury that they in determining the value of that time they could take into account the profit potential in the agents’ territory.225

Some courts gave Griffin a slightly different interpretation. The Griffin opinion said:

Cases not unfrequently occur in which . . . it is certain that some loss has been sustained or damage incurred, and that such damage is the direct, immediate, and natural consequence of the breach of the contract or duty, but where the damage may be estimated in various ways. In all such cases the law . . . uniformly adopts the mode of estimating damages which is most definite and certain.224

This could be read to mean that if there is one method (such as the awarding of lost profits) that is most likely to put the plaintiff in the position they would have been in but for the breach of the contract or duty and a second method where the calculation is subject to less inaccuracy or uncertainty, the court should always adopt the latter. This may have been the reasoning some cases that quoted and relied on this language from Griffin.225 But most of these cases seem to have thrown this in as additional authority where the lost profits were too uncertain to be recovered.226 One example is a case that eerily parallels the facts of Hadley v. Baxendale. In Southern Railway Co. v. Coleman,227 a cotton gin was shut down because of a broken press pin. The owner of the gin delivered the pin to the Southern Railway, which was to carry it to an iron works at Selma, Alabama, 56 miles away, where it was immediately to be repaired and returned to the ginner. 228 Unlike the famous ambiguity in the Hadley opinion,229 there was no

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160 Ill. App. 554, 564 (Ill. Ct. App. 1911) (relying on Griffin to award rental value of plaintiff’s plant where construction was delayed because of fault of defendant).

In Brownell & Co. v. Chapman, 51 N.W. 249, 250 (Iowa 1892) the court noted that some cases had adopted the interest that could have been earned on the capital invested in the property as the measure of damages, but it said that the rental value rule far outweighed it in “the number of cases and the reasoning supporting the rule.” The opinion quoted Griffin.


223 See Howe Mach. Co. v. Bryson, 44 Iowa 159, 162-64 (Iowa 1876).

224 16 N.Y. at 495.

225 E.g., St. Louis & San Francisco R.R. Co. v. Lilly, 55 So. 937 (Ala. Ct. App. 1911).


227 444. So. 837 (Ala. 1907).

228 See id. at 838.
question that the ginner had told the railroad agent “that his ginnery ‘would be at a standstill’ until the pin should be repaired and returned.” Nevertheless, through the negligence of the railroad employees the pin was not delivered to the iron works for seven days and then only because the plaintiff himself went to Selma and located the pin in a railroad car. The pin was then repaired within three hours and returned to the gin the next day. The plaintiff sued to recover the profits lost during the time the gin was shut down on account of the railroad’s negligence. The plaintiff said that his profit was 75 cents for each bale of cotton ginned, but he could not give a good estimate of the number of bales lost. In spite of this, trial judge charged the jury that he was entitled to recover his lost profits. The Alabama Supreme Court, however, reversed the award of lost profits. Its opinion quoted Griffin’s statement that the law adopts “the mode of estimating damages which is most definite and certain.” It concluded that if the period of the delay was long enough for the gin to have had an ascertainable rental value for that period, then that rental value would be the appropriate measure of damages. If there was no ascertainable rental value for such a short period, then the damages would be the interest on the value of the gin.

C. The Tacit Agreement Test

Another roadblock on the highway to a rule allowing the recovery of lost profits was the rule of Hadley v. Baxendale. Although the modern reading of Hadley is that lost profits need only to have been foreseeable at the time the contract was made, courts in many American jurisdictions adopted the so-called “tacit agreement test.” Under this test, a party seeking to recover lost profits (or any other consequential damages) had to do more than simply show that the defendant had notice of the special circumstances giving rise to the damages. They had to show that the defendant had manifested (expressly or impliedly) an intent to assume the risk of those damages. This rule apparently originated in England shortly after Hadley. Most accounts trace it back to British Columbia Saw-Mill Co. v. Nettleship, an English opinion of 1868. The defendant had contracted to transport machinery for a sawmill from Glasgow to Vancouver. One of

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229 The facts of the case as related by the reporter say that the plaintiffs’ servant told the defendant’s clerk that the shaft must be sent immediately because the mill was stopped. See 156 Eng. Rep. at 147. Baron Alderson’s opinion, however, says that the clerk had no way of knowing whether the mill was stopped. See id. at 151.

230 See 444 So. at 838.
231 See id. at 838.
232 See id. at 838.
233 See id. at 839.
234 See id. at 839.
235 See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 351 (“Damages are not recoverable for loss that the party in breach did not have reason to foresee as a probable result of the breach when the contract was made.”).
236 CALAMARI & PERILLO, supra note 6, § 14.5(a).
237 3 C.P. 499, 500 (1868).
the boxes, which contained many small and important items, failed to arrive at Vancouver.\textsuperscript{239} It took nearly a year for replacement parts to arrive from Britain, during which time the sawmill was idle.\textsuperscript{240} The jury awarded damages of 3,000 pounds, the bulk of which (2646l. 2s. 3d.) was the rental value of the whole of the machinery (not even the rental value of the sawmill, let alone the lost profits from the sawmill).\textsuperscript{241} The court of common pleas, however, reduced the damages to 353l. 17s. 9d., the cost of replacing the missing parts, including freight to British Columbia.\textsuperscript{242} In his opinion, Bovill, C.J. said:

The extent of the carrier’s liability is to be governed by the contract he has entered into, and the obligations which the law places upon him. He is not to be made liable for damages beyond what may fairly be presumed to have been contemplated by the parties at the time of entering into the contract. It must be something which could have been foreseen and reasonably expected, \textit{and to which he has assented expressly or impliedly by entering into the contract}.\textsuperscript{243}

The leading American authority for the tacit agreement test was Justice Holmes’ 1903 opinion in \textit{Globe Refining Co. v. Landa Cotton Oil Co.}\textsuperscript{244}

Another impediment to recovering lost profits was that courts of the day seemed unwilling to assume that a party making a contract to supply goods or services would foresee that its buyer intended to earn a profit through the use or resale of those goods or services.\textsuperscript{245} For example, in 1891, defendants who were being sued on a note for the purchase price of sawmill machinery attempted to set off the profits they lost because the machinery had been delivered two months late.\textsuperscript{246} Their lawyers, undoubtedly having read \textit{Hadley v. Baxendale} very carefully, included in their plea an allegation that the plaintiff’s knew the mill was stopped on account of the non-delivery of the machinery.\textsuperscript{247} The Alabama Supreme Court nevertheless held that the plea was “bad” because there was

\begin{footnotesize}
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\item See id. at 500.
\item See id.
\item See id. at 501.
\item See id. at 505.
\item Id. at 505-06 (emphasis supplied). In his concurring opinion, Judge Willes, said that the question of consequential damages was a difficult one and described a case from 250 years earlier in which a man who was travelling to be married to an heiress had a horseshoe replaced on the journey. The blacksmith who replaced it did such a bad job of it that the horse became lame, the groom did not arrive on time and the woman married someone else. See id. at 508. If the judges considered the case even remotely similar to the one before it, it is easy to understand why they decided as they did. Interestingly, the first Restatement of Contracts, which rejected the tacit agreement test, used this fact situation as an example of a situation where the breaching party would clearly \textit{not} be liable. \textit{RESTATEMENT OF CONTRACTS}, § 330, ill. 8 (1932).
\item 190 U.S. 540 (1903).
\item See, e.g., Harvey v. Conn. & Passumpsic R.R. Co, 124 Mass. 421, 423-25 (Mass. 1878) (shipper could not recover profits lost on contracts to make lumber into railroad ties because it had not informed railroad of the contracts at the time it made the contracts for shipment); Thomas, Badgley & Whitworth Mfg’g Co. v. Washbash, St. L. & Pac. Rw. Co., 22 N.W. 827 (Wis. 1885) (shipper could not recover for loss of use of machine damaged during shipping because railroad not informed of use of machine).
\item Reed Lumber Co. v. Lewis, 10 So. 333, 334 ( Ala. 1891).
\item See id.
\end{enumerate}
\end{footnotesize}
no allegation that the plaintiffs knew the defendants had contracts to sell the lumber from the mill at a profit.\textsuperscript{248}

In a 1901 case, \textit{Acme Cycle Co. v. Clarke},\textsuperscript{249} the Indiana Supreme Court held that a trial court had been correct in refusing to award a bicycle manufacturer the profits lost on account of the late delivery of machinery necessary to manufacture the hubs for its bicycles. The court said that even if the bicycle company should have notified the machinery supplier that it had the ability to manufacture an additional 500 bicycles a month if it had the hub machines and that it could sell those bicycles at a profit, it would not have been enough to meet the requirements of \textit{Hadley v. Baxendale} (and \textit{Griffin v. Colver}, which the court cited along with \textit{Hadley} for the foreseeability requirement\textsuperscript{250}). According to the court:

The later English cases indicate that where extraordinary liabilities are to be assumed by a party contracting to deliver goods, it should appear that he understood the nature of the responsibility he was taking upon himself, and that his compensation should include some consideration for the responsibility assumed. Furthermore, these cases intimate that the liability of the party for the extraordinary damages, which might result from a breach of the contract to deliver, should be so plainly understood as to render it one of the terms of the contract that, in case of a failure to deliver the goods, the person guilty of the breach would be responsible for such damages. And the very reasonable observation has been made that, if parties desire to avail themselves of a claim to such damages, they should expressly stipulate for them in the contract itself.\textsuperscript{251}

This combines the rationale of the tacit agreement test with the assumption that the defendant would not expect that the plaintiff intended to use the goods in a profit-making endeavor.

In 1891, the United States Supreme Court had said: “The authorities both in England and the United States are agreed that as a general rule, subject to certain well-established qualifications, the anticipated profits prevented by breach of are not recoverable in the way of damages for such breach . . . .”\textsuperscript{252} Citing the 1880 edition of \textit{Sedgwick on Damages}, the court listed three reasons this was so:

(1) that in the greater number of cases such expected profits are too dependent upon numerous [sic], uncertain and changing contingencies to constitute a definite and trustworthy measure of actual damages; (2) because such loss of profits is ordinarily remote and, as a matter of course, the direct and immediate result of the

\textsuperscript{248} \textit{See id.}
\textsuperscript{249} 61 N.E. 561.
\textsuperscript{250} Although \textit{Blanchard v. Ely} has been overlooked as an early case requiring that damages for breach of contact be foreseeable (see \textit{supra}, Part III), \textit{Griffin v. Colver} was often in the late eighteenth and early nineteenth centuries cited for that rule. \textit{See, e.g.}, \textit{Hagen v. Rawle}, 143 Ill. App. 543 (Ill. Ct. App. 1908).
\textsuperscript{251} \textit{Id.} at 563.
\textsuperscript{252} \textit{Howard v. Stillwell & Bierce Mfg’g Co.}, 139 U.S. 199, 205-06 (1891).
non-fulfilment of the contract; (3) and because most frequently the engagement to pay such loss of profits, in case of default in the performance, is not part of the contract itself, nor can it be implied from its nature and terms.\textsuperscript{253}

The first of these reasons we would express today by saying that the plaintiff had failed to prove its damages with reasonable certainty.\textsuperscript{254} The second shows the courts’ unwillingness to assume that the breaching party should have expected that the other party had plans to use the goods and services in question to make a profit, and the third presages the Court’s adoption of the tacit agreement test.

This idea that the breaching party would not expect the plaintiff to have plans to earn profits on what it had expected to buy continued well into the twentieth century. As late as 1934, Professor McCormick could write about “the rule which denies recovery for unusual consequences of a breach of contract, where knowledge of the risk is not brought home to the defendant” and go on to say that the most frequent of these “unusual consequences” was loss of profits on a contract to resell the goods contracted for. \textsuperscript{255} Professor Bauer went even further, saying that even though Williston’s treatise on contracts (the leading work on contracts of that era) said that consequential damages could be awarded if the defendant was on notice of special circumstances, there were few cases it cited in which the plaintiff recovered without evidence that the defendant intended to assume liability for the consequences of those special circumstances.\textsuperscript{256}

Even as McCormick wrote, however, things were beginning to change. Courts were beginning to allow plaintiffs to recover consequential damages without showing they had put the defendant on notice they intended to earn a profit with the goods (or occasionally, services) contracted for.\textsuperscript{257} McCormick himself suggested that judges interpreted the contemplation requirement flexibly, finding the lost profits within the contemplation of the parties when they thought it fair to allow recovery of the lost profits and finding they were not contemplated when the court thought their recovery would be unfair.\textsuperscript{258}

The drafters of the first Restatement of Contracts (Professor Williston was the Reporter) took a position seemingly opposite to that of most of the case law when they said in a comment to section on the Hadley \textit{v.} Baxendale rule:

A seller or carrier of goods usually has reason to know that the buyer or shipper either has made or will probably make a contract for the sale of the goods at a reasonable profit. Such circumstances are in the usual course of things. He therefore has reason to foresee that his own failure to deliver

\textsuperscript{253} Id. at 206.
\textsuperscript{254} See, e.g., \textsc{Restatement (Second) of Contracts} § 347 (1989).
\textsuperscript{255} McCormick, supra note 4, \textsc{Minn. L. Rev.} at 504.
\textsuperscript{257} See, e.g., Bonhard \textit{v.} Gindin, 142 A. 52, 55 (N.J. 1928) (allowing recovery of lost profits which plaintiff intended to make on resale of property without proof that that defendant had actual knowledge of intent to resell; \textit{Hadley v. Baxendale} cited).
\textsuperscript{258} See McCormick, supra note 4, \textsc{Minn. L. Rev.} at 508.
the goods as agreed will prevent the plaintiff from making such a reasonable profit.\footnote{259}  

The Restatement also rejected categorically the tacit agreement test.\footnote{260} What is probably more important, the Restatement expressed the \textit{Hadley} test in terms of the defendant being liable those injuries that he “had reason to foresee” as a result of the breach.\footnote{261} Although this is a subtle change from the language generally used before, in which it was said that the injury had to be “in the defendant’s contemplation,” it is an important one. It implies that the plaintiff can recover if the defendant, at the time it made the contract, had reason to expect that the plaintiff would lose profits if the defendant breached. The defendant did not have to be thinking about, or “contemplating” the loss of profits; it just had to be in a position where, \textit{if} it had thought about the issue, it should have realized there was a good chance that a breach would lead to a loss of profits. The Uniform Commercial Code took a similar position. A comment said that the standard was whether the seller “had reason to know” of the potential damages.\footnote{262}  

These developments contributed to a general relaxation of the foreseeability requirement that began about 1930. The current attitude is reflected in cases such as \textit{Burnett and Doty Development Co. v. Phillips}.\footnote{263} There, the California Court of Appeals held that the fact a builder personally added a completion date into a subcontract was enough to make it foreseeable that the builder would suffer lost profits when the subcontractor failed to complete its work on time.\footnote{264} In \textit{Manouchehri v. Heim},\footnote{265} the New Mexico Supreme Court allowed a physician to recover the profits he lost as a result of a defective x-ray machine. The seller argued that these lost profits were not foreseeable, but the court rejected this argument, saying: “[The defendant] knew his customer and knew how the x-ray machine was to be used. Any reasonable person in his position would assume that doctor using such a machine would charge more for its use than the cost of operation and would earn income from it.”\footnote{266} Similarly, when Virginia Polytechnic Institute (Virginia Tech) breached a contract to work with a private corporation to jointly develop new technology, it was foreseeable from the nature of the enterprise that the parties would receive profits from the licensing or sale of the technology.\footnote{267}  

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\footnote{259} Restatement of Contracts § 330 cmt. c (1932).  
\footnote{260} See id. cmt. a (“One who has committed a breach of contract is bound to pay damages only for such injury as he had reason to foresee when he made the contract. This does not mean, however, that the defendant must have had the resulting injury actually in contemplation or that he promised either impliedly or expressly to pay therefore in case of breach.”)  
\footnote{261} Id. § 330.  
\footnote{262} U.C.C. § 2-715, official comment 2 (internal quotations omitted).  
\footnote{263} 148 Cal. Rptr. 569 (Cal. Ct. App. 1978).  
\footnote{264} See id. at 572.  
\footnote{265} 941 P.2d 978 (N.M. 1997).  
\footnote{266} Id. at 983.  
\end{footnotesize}
A few jurisdictions, most notably New York, still cling to the tacit agreement test, and in those jurisdictions the Hadley principle is still an important limitation on a plaintiff’s ability to recover lost profits, though even in those jurisdictions the certainty requirement is much more important.

This leaves open one question in the development of the reasonable certainty rule. How did the courts transform the requirement that the lost profits be proven with absolute certainty to one that they be proven with “reasonable certainty?” The language of Griffin v. Colver was ambiguous on this score. In the second paragraph of the opinion, Judge Selden says that “[i]t is a well established rule of common law that the damages to be recovered for a breach of contract must be shown with certainty.” Later in the opinion in language that has been incorporated into many opinions in many jurisdictions, he says that the damages “must be certain; both in their nature and in respect to the cause from which they proceed.” But here it is not clear that when he speaks of certainty he means absolute certainty rather than reasonable certainty because he contrasts “certain” with “speculative,” indicating that a reasonable estimate may be all that is required. More importantly, two paragraphs later, he says that “the law . . . uniformly adopts that mode of estimating the damages which is most definite and certain.” This clearly implies that some uncertainty is to be tolerated.

Some twentieth century courts have said that Griffin stated a requirement of absolute certainty that later was transformed into the less demanding requirement of reasonable certainty. But the courts of Griffin’s time seem to have begun stating the requirement as one of reasonable certainty as soon as they began relying on Griffin to allow the recovery of lost profits. An 1883 opinion of the Minnesota Supreme Court cited Griffin for the proposition: “To enable loss of profits to be shown on a question of damage, they should, for obvious consideration, be reasonably certain, otherwise any estimate of damages based upon them is conjecture.” A year earlier, the Iowa Supreme Court, though not citing Griffin, talks of tracing the loss “with reasonable certainty to the breach of the contract.” Similarly, Maryland’s highest court, after citing Griffin, said: “the plaintiff must establish the quantum of his loss by evidence from which the jury will be able to estimate the extent of his injury, excluding all elements of injury as are

269 16 N.Y. at 491.
270 Id. at 495.
271 See id.
272 Id.
274 See, e.g., Cent. Coal & Coke Co. v. Hartman, 111 F. 96, 98 (8th Cir. 1901)(citing Griffin for the proposition that profits of a commercial enterprise generally cannot be recovered because they cannot be proven with reasonable certainty); Hunt v. Ore. Pac. Ry. Co, 36 F. 481, 484 (D. Ore. 1888)(citing Griffin for requirement that damages be proven with reasonable certainty).
275 Cushing v. Seymour, Sabin & Co., 15 N.W. 249, 250 (Minn. 1883).
incapable of being ascertained to a reasonable degree of certainty by the usual rules of evidence.” 277

VII. CONCLUSION

It is impossible to overstate the importance of three now-forgotten New York opinions—Blanchard, Masterton, and Griffin. They brought into American law the foundation for damages in commercial disputes: Lost profits may be recovered, but only if they are proven with reasonable certainty. Law students may be tortured with the Court of the Exchequer’s opinion in Hadley v. Baxendale, and academics may write endless articles about whether the rule that case articulated is economically efficient, 278 but in significant commercial litigation, it is the rule of Griffin v. Colver that determines the outcome.

277 29 A. 1036, 1038 (Md. 1894).