THE SCOPE OF THE CONTRACT*

AFFIRMATIONS OR PROMISES MADE IN THE COURSE OF CONTRACT NEGOTIATIONS

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A. The Scope of the Problem

Law Reform has lately become a popular cause, not merely with lawyers, but also with legislators and with other sections of the community. In these circumstances lawyers have a peculiar responsibility to see that the efforts of the reformers are well directed to the real maladies. This paper is a plea for recognition of the need for re-examination of some of the more fundamental aspects of law to determine whether they are adequate to meet today's needs and to solve contemporary problems.

It is suggested that this is a time when lawyers in Australia should be keenly and critically examining some of the basic principles of the law of contract. Such an examination has recently taken or is currently taking place in many jurisdictions, and it would be unfortunate if Australian lawyers were not to play their part in the exercise. In America, most of the States have now adopted the provisions of the Uniform Commercial Code, which has not hesitated to re-fashion established concepts where these were not considered to be working satisfactorily. There have been international conventions on a 'Uniform Law on the International Sale of Goods' and a 'Uniform Law on the Formation of Contracts for the International Sale of Goods.' In England, the Misrepresentation Act 1966 gives effect to the recommendations of the Law Reform Committee,[1] and the codification of the law of contract figures prominently in the first programme of the new Law Commission. In New Zealand, a sub-committee of the Law Revision Committee has been working for some time on the reform of aspects of the law of contract and the law relating to sale of goods, and it is hoped that its report will be available shortly. The programme of the New South Wales Law Reform Commission dated 1st September 1966 includes the 'review of the Law of Contract with a view to its codification.'

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[1] Tenth Report, (1962). *Cmnd.* 1782.

The law relating to the formation of contracts—particularly as to the recognition of the existence of a contractual nexus and as to the identification of the terms of the contract—seems to be an area that is ripe for reappraisal. It seems no difficult matter in this field to state what the law is, and to formulate from the authorities certain rules for the determination of problems that arise. The difficulty lies in the application of these rules to factual situations in anything other than an arbitrary manner. The established rules presuppose a process of negotiation that frequently bears little resemblance to reality except perhaps in relation to contracts for the sale of land and other formally negotiated contracts. The actual process of negotiation has therefore to be expressed by lawyers in a mould which is often inappropriate to reflect the real agreement of the parties. The majority of modern contracts are not negotiated according to a strict formula of offer, rejection, counteroffer, and acceptance, but either there is a simple agreement, e.g. to buy and to sell a specified or generically described article, and everything else is left to the implication of the law, or else there is the production of standard forms by one or both parties, but the agreement is concluded and performed without either party giving thought or acquiescence to the proferred 'terms' of the other, and frequently on the basis of conflicting sets of terms. To unravel these knots, it is submitted that established rules are inadequate, and not infrequently produce a contract some way removed from the actual 'consensus' of the parties.[2]

In this article it is proposed to assume that the existence of a contract between the parties has been established, and to examine some of the problems encountered in determining what are the *express* terms of that contract. Difficulties arise because the actual point of time at which it can be averred that the parties have become contractually bound to one another may well have been preceded by a period of negotiation or 'dickering' during which both parties will have made statements of their requirements and expectations, affirmations of fact, and various promises, and it will need to be determined how much of what they have said or written has been caught up into the contract. A statement made during the course of negotiations which is called into issue by subsequent events will need to be classified to determine the legal consequences if the expectations it gave rise to are not fulfilled.[3] The method of making this classification and the legal consequences that flow from it are the problems under review.

It should be stressed by way of introduction that a study of the case law in this field does not reveal very many instances of which one could

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[2] This problem of finding the agreement through the 'Battle of the Forms' has been discussed by the writer in 1 *Business and Law* (Journal of the New Zealand Business Law Association) 45.

[3] Such a statement may also reflect or give rise to an operative mistake, but it is not proposed in this paper to add to the complexity by exploring this aspect of the problem.

say that clearly injustice had been done (or that it had not been possible to do substantial justice between the parties) because of the inadequacies or rigidity of the law.[4] That this is so is no doubt a tribute to the courts rather than to the law. In many cases one is left with the impression that on the evidence it would have been as easy for the court to hold that a statement was made *animo contrahendi* as that it was not, to hold that a term was a condition as that it was a warranty, or to invoke the notion of collateral contracts as to reject it. It may frequently be tempting to conclude that a court has first decided a particular case simply upon its merits and then classified the statement involved in accordance with these merits to reach the desirable result. Courts should not however be forced into artificial casuistry in order to do justice; and each new decision adds a further precedent to the law until a body of highly technical distinctions has been amassed which renders the task of advising clients a fine exercise in speculation. At this point it becomes necessary to clear the minefield and return to principle—and this is just what appears to have been happening in the most recent cases.[5] But if the principles are the same as before, one may be excused for wondering whether the process can help but repeat itself. The need is for a re-examination of principle.

B. Finding the Express Terms

The traditional approach to the problem of statements (whether affirmations or promises) made in the course of negotiations is to enquire whether they have become terms of the contract or are mere representations inducing the contract but not properly part of it. If they are terms of the contract, it must then be asked whether they have the status of conditions or warranties. If they were conditions, until recently it seemed essential to go further and enquire whether they were 'something narrower than a condition of the contract'[6]—*i.e.* 'the core of the contract'—because if so their breach was not capable of being excused by an exclusion clause, no matter how widely drawn. However, as a result of recent decisions, notably of the High Court in *Council of the City of Sydney* v. *West*[7] and of the House of Lords in *Suisse Atlantique Societe D'Armement Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale*,[8] it now appears that there may be no such rule of law automatically striking out exclusion clauses but that the

[4] A case in which it is submitted that a rigid application of established rules did produce injustice is *Rose Ltd.* v. *Pim & Co. Ltd.* [1953] 2 Q.B. 450. This case is discussed further at p. 247 *infra*.

[5] See for example *U.G.S. Finance Ltd.* v. *National Mortgage Bank of Greece* [1964] 1 Lloyd's Rep. 446, 453 per Pearson L.J.; *Hardwick Game Farm* v. *Suffolk Agricultural and Poultry Producers Association Ltd.* [1966] 1 All E.R. 309; *Suisse Atlantique Societe D'Armement Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale* [1966] 2 W.L.R. 944; *Council of the City of Sydney* v. *West* (1965) 39 A.L.J.R. 323.

[6] Per Devlin J. in *Smeaton Hanscomb & Co. Ltd.* v. *Sassoon I. Setty & Co.* [1953] 2 All E.R. 1471, 1473.

[7] (1965) 39 A.L.J.R. 323.

[8] [1966] 2 W.L.R. 944.

question is simply one of construing the clause in the light of the whole contract to determine whether or not it applies in the circumstances that have occurred.[9]

The two remedies of rescission[10] and damages have to be distributed among these various categories of affirmations. Hence, if the affirmation is found not to be contractual but a 'mere puff', or if it exceeds 'puffing' but had not induced the contract, the party to whom it was made will have no remedy. If the affirmation, whilst still not contractual, nevertheless was factual and induced the contract, the innocent party will be entitled to rescission[11] (subject to various bars) if the representation were made innocently, and rescission and/or damages if it were made fraudulently. On the other hand, if the statement is contractual and is found to be a warranty, the only remedy is damages; whereas if it amounts to a condition the innocent party may rescind (subject to loss of this right in certain circumstances) and/or claim damages. It is therefore of prime importance to both parties how this initial classification is made.[12] As the whole purpose of the classification is to allocate remedies, one would expect to find here some clear principle. Is rescission regarded as a more drastic remedy than damages, or vice versa? One may search in vain for an answer.

The Traditional Method of Making the Classification

Mere Representation or Term: Subject to the overriding rule that, where the parties have purported to reduce the whole of their contract to writing, parol evidence may not be adduced to add to, vary or contradict the writing,[13] whether or not a statement is contractual depends on the intention of the parties. There must be a finding of *animus contrahendi* in relation to the particular statement. 'An affirmation at the time of sale is a warranty, provided it appear on evidence

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9 The problem raised by these cases is discussed in more detail at p. 242 *et seq. infra.*

10 There are important, if somewhat obscure, distinctions between rescission on account of matters in the formation of the contract and rescission for breach. See generally *Salmond & Williams on Contract* (2nd ed.) 564-571, and also *McDonald* v. *Dennys Lascelles Ltd.* (1933) 48 C.L.R. 457, 476 per Dixon J.

11 This of course is subject to doubts whether, on a strict interpretation of the Sale of Goods Act 1896 (Tas.), s. 5(2), the remedy of rescission for innocent misrepresentation is available on a contract for the sale of goods. See *Re Wait* [1927] Ch. 606, 635-636 per Atkin L.J.; *Watt* v. *Westhoven* [1933] V.L.R. 458; *Riddiford* v. *Warren* (1901) 20 N.Z.L.R. 572.

12 The cases reveal much manoeuvring for position. Hence, for the plaintiff who wishes to rescind, it may be better to keep the statement at the level of a mere representation rather than plead it as a term of the contract unless he is sure that, so pleaded, it can be elevated to the status of a condition. Whereas, for a defendant who may wish to resist a claim for rescission, it is important (unless he can establish some bar to rescission) to peg the statement as a warranty, no more and no less, or, if he wishes to resist damages, to keep it out of the contract entirely (and then establish the bar to rescission).

13 See, for example, *Jacobs* v. *Batavia and General Plantations Trust* [1924] 1 Ch. 287 and *Clough* v. *Rowe* (1888) 14 V.L.R. 70.

to have been so intended'.[14] 'The intention of the parties governs in the making and in the construction of all contracts'.[15]

However, the test of intention is necessarily objective, so that the question tends to become not 'What did the parties intend?' but 'What, on the totality of the evidence, must they be taken to have intended?'[16] The emphasis therefore shifts from the thoughts of the parties to their conduct and to the importance which the court thinks should be attached to the particular statement in the context of the particular transaction.

Warranty or Condition: The modern distinction here is generally considered as being between 'minor' and 'major' terms of the contract. The definition of warranty in the Sale of Goods Act,[17] and of warranty and condition by Blackburn J. in *Bettini* v. *Gye*[18] and by Fletcher Moulton L.J. in *Wallis, Son and Wells* v. *Pratt and Haynes*[19] is in terms that a warranty is collateral to the main purpose of the contract, whilst a condition goes to the root or essence of the contract. However, it is clear that whether a term is to be regarded as collateral or as going to the root again depends on the parties' intentions, and again this is to be determined by objective standards.[20] As with the question whether or not the statement is contractual, the test becomes one of relative importance gauged objectively. 'You look at the stipulation broken from the point of view of the probable effect or importance as an inducement to enter into the contract'.[21]

The result of this traditional approach is that, if to mere representation, warranty, and condition there is added the 'core of the contract', there are four grades of relative importance of affirmations on which the rights of the parties and the availability of substantially two remedies are made to depend. A reading of the cases can only leave one with the impression that the test is unworkable and the decision as to the grade of importance arbitrary. Too often the court appears to decide whether the remedy sought would be appropriate in all the circumstances, and then classifies the statement appropriately; and one is left with no more reason than the bald assertion that it does or does not appear that the importance of this statement to the parties was such as to justify the relief sought. In most of the cases it is difficult to see

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14 *Pasley* v. *Freeman* (1789) 3 Term R. 51, 57 per Buller J.

15 *Bannerman* v. *White* (1861) 10 C.B.N.S. 844, 860 per Erle C.J. See too *Hopkins* v. *Tanqueray* (1854) 15 C.B. 130; *Heilbut, Symons & Co.* v. *Buckleton* [1913] A.C. 30; *Thomas* v. *Nelson* (1920) 20 S.R. (N.S.W.) 579.

16 *Heilbut, Symons & Co.* v. *Buckleton* [1913] A.C. 30, 51; *Oscar Chess Ltd.* v. *Williams* [1957] 1 All E.R. 325, 328; *Dick Bentley Productions Ltd.* v. *Harold Smith (Motors) Ltd.* [1965] 2 All E.R. 65, 67.

17 Sale of Goods Act 1896 (Tas.) s. 3; and see s. 16(2).

18 (1876) 1 Q.B.D. 183.

19 [1910] 2 K.B. 1003, 1012.

20 *Bentsen* v. *Taylor, Sons & Co.* [1893] 2 Q.B. 274, 281 per Bowen L.J.; *Bowes* v. *Chaleyer* (1923) 32 C.L.R. 159, 177-183 per Isaacs and Rich JJ.; *A.-G.* v. *Australian Iron & Steel Ltd.* (1936) 36 S.R. (N.S.W.) 172; *Francis* v. *Lyon* (1907) 4 C.L.R. 1023, 1034; *Associated Newspapers Ltd.* v. *Bancks* (1951) 83 C.L.R. 322, 336.

21 C. B. Morison: *Principles of Rescission of Contracts* (1916) 86.

how more reason than that could be given to justify what has inevitably come to depend in large measure on the subjective reaction of the judge.

The Breakdown of the Traditional Method

Mere Representation or Term: Whilst actions of this nature were tried uniformly as jury actions, it was probably not necessary to ask very seriously whether the test of intention was subjective or objective. However, as juries have ceased to be used regularly in this type of case in most jurisdictions (and as the volume of dicta from appellate cases has increased), not only has this question assumed importance, but the test of intention has itself been weakened. Under strict orthodoxy, if the contract is entirely written, the only question that can arise is whether terms are conditions or warranties and this is purely a question of construction for the judge. On the other hand, if the contract is entirely oral and the question is whether or not oral representations are terms (and if so, whether they are conditions or warranties), this, turning as it does purely on intention, is a question of fact for the jury, subject to the power of the judge to rule on the sufficiency of evidence. But where the contract is partly written and partly oral, in spite of some confusion in the cases, it is submitted that this is still a question of fact for the jury, subject first to a ruling by the court (if necessary) that the writing is not intended to be exclusive, and also subject to the power of the court to withdraw the matter from the jury if there is insufficient evidence.[22] However, when these issues arise before a judge sitting alone or before appellate courts, questions of sufficiency or relevancy of evidence assume the appearance of ancillary rules explaining and expounding the test of intention, and matters of evidence tend to become rules of construction.

The House of Lords in *Heilbut, Symons & Co.* v. *Buckleton*[23] affirmed in clear tones that the prime test was intention, and disapproved

[22] *Hopkins* v. *Tanqueray* (1854) 15 C.B. 130 (no evidence of warranty to go to jury); *Couchman* v. *Hill* [1947] K.B. 554, 558 per Scott L.J.: '. . . the only inference that could properly be drawn by the judge or jury charged with the duty of finding the facts—and this is a question of fact as to the intention of the parties—. . . .'; followed by the Court of Appeal in *Harling* v. *Eddy* [1951] 2 K.B. 739 (but without inquiry whether fact or law); *Heilbut, Symons & Co.* v. *Buckleton* [1913] A.C. 30, 36 per Viscount Haldane L.C.: 'When evidence has been properly submitted to the jury, that body is entrusted with a duty which in large measure limits the province of the judge. If there was evidence on which the jury could properly find, its finding cannot be set aside, merely because if the court had been dealing with that evidence the court would have found otherwise. . . . But the question always remains whether the evidence was, so far as the relevant issue is concerned, of a character so insufficient as to render it wrong in law for the judge to have submitted it to the jury as material on which to base a finding on that issue . . . *as neither the circumstances of the conversation nor its words were in dispute,* I think that the question of warranty or representation was one purely of law and that it ought not to have been submitted to the jury'. (emphasis supplied); compare Lord Atkinson, *ibid.* 43: 'The existence or non-existence of such an intention in the mind of the party making the affirmation, that his affirmation should be taken as a warranty of the truth of the fact affirmed, is, in an action of breach of warranty, no doubt a question for the jury which tries the action. . . .' See too *Thomas* v. *Nelson* (1920) 20 S.R. (N.S.W.) 579, and *Criss* v. *Alexander* (1928) 45 W.N. (N.S.W.) 76, 78 per Campbell J.

[23] [1913] A.C. 30.

of the dictum of the Court of Appeal in *De Lassalle* v. *Guildford*[24] that the decisive test was whether the representor purported to assert a fact of which the representee was ignorant or merely to state an opinion or judgment on a matter of which the representor had no special knowledge and on which the representee might be expected to have his own opinion and exercise his own judgment. In spite of this, English courts at any rate have in recent years clearly relied on the fact of special knowledge as an ancillary test, and have advanced the notion that, in the absence of any clear indication of intention either way (which is usually the case), a statement during negotiations is a term of the contract if the person making it had or could reasonably have obtained the information to show whether the statement was true or false. So, in *Routledge* v. *McKay*[25] on the oral sale of a motor-cycle the seller wrongly stated the age of the vehicle, relying innocently on a false entry on the registration book. It was held by the Court of Appeal that, as the seller had merely passed on a statement the accuracy of which he was unable to verify, he could not be considered to have warranted it and the statement was therefore merely an innocent misrepresentation. Similarly, in *Oscar Chess Ltd.* v. *Williams*[26] the seller traded in a car to a dealer from whom he was purchasing a new car. Relying, as in *Routledge's* case, on the registration book he represented it as a 1948 model, whereas in fact it was a 1939 car. Denning and Hodson L.JJ. held that lack of knowledge on the part of the seller made his statement merely an innocent misrepresentation and not a warranty. Morris L.J., dissenting, considered that as the representation was made at the time of contracting it was an integral part of the oral contract, and that as its importance was obviously so great in determining the trade-in allowance, it was fundamental to the transaction and should be regarded as a condition. He affirmed the test laid down by the House of Lords in *Heilbut, Symons & Co.* v. *Buckleton.* This difference of opinion in the Court of Appeal neatly illustrates the varying approaches to the problem.

The matter was carried a stage further by Lord Denning in *Dick Bentley Productions Ltd.* v. *Harold Smith (Motors) Ltd.*[27] In that case the defendant's salesman represented to the buyer that he was in a position to ascertain the history of a car, that the car had been fitted with a replacement engine and gearbox, and that the car had done only 20,000 miles since then. Lord Denning, M.R. (with whose judgment Danckwerts and Salmon L.JJ. agreed) said that the test was intention but that this test was difficult to apply.

> . . . if a representation is made in the course of dealings for a contract for the very purpose of inducing the other party to act on it, and it actually induces him to act on it by entering into the contract, that is *prima facie* ground for inferring that the representation was a warranty. . . . but the maker

24 [1901] 2 K.B. 215, 221.
25 [1954] 1 All E.R. 855.
26 [1957] 1 All E.R. 325.
27 [1965] 2 All E.R. 65.

> of the representation can rebut this inference if he can show that it really was an innocent misrepresentation, in that he was innocent of all fault in making it, and that it would not be reasonable in the circumstances for him to be bound by it [as in *Oscar Chess Ltd.* v. *Williams*].[28]

Whatever the practical merits of this approach may be, insofar as it raises a presumption of warranty in the absence of proof of moral innocence on the part of the representor, it is difficult to reconcile with the primacy of intention as asserted by the House of Lords in the earlier decisions.[29]

Warranty or Condition: In determining whether an acknowledged term is a condition or warranty of the contract, a similar erosion of the test of intention is observable and a number of 'ancillary tests' have been proposed. Hence,

> . . . the test to be applied in determining whether a term of a contract is to be construed as being essential or vital is to consider whether in the absence of its observance the other contracting party would get something different in substance from what he contemplated by his bargain.[30]

> The test of essentiality is whether it appears from the general nature of the contract considered as a whole, or from some particular term or terms, that the promise is of such importance to the promisee that he would not have entered into the contract unless he had been assured of a strict or a substantial performance of the promise . . . and that this ought to have been apparent to the promisor.[31]

Far more significant on this point, however, is the tendency of a number of recent cases to deny even the existence of the condition/warranty dichotomy. According to this approach, the remedies on breach available to the innocent party depend not upon an initial classification of the importance of the term breached, but upon the significance of the events that actually result from the breach. The question of remedies is assigned where, it is submitted, it properly belongs, namely to the topic of breach rather than to formation of the contract.

This approach was enunciated most clearly by Diplock and Upjohn L.JJ. in *Hong Kong Fir Shipping Co. Ltd.* v. *Kawasaki Kisen Kaisha Ltd.*[32] In that case the Court of Appeal held that the unseaworthiness of a vessel and the consequent delay, although breaches of contract, did not of themselves entitle the innocent party to repudiate the charter unless they were so great as to frustrate the commercial purpose of the

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28 *Ibid.* 67.

29 Other 'ancillary tests' are discussed in Cheshire and Fifoot: *Law of Contract* (Aust. ed.) 200, 203.

30 *A.-G.* v. *Australian Iron & Steel Ltd.* (1936) 36 S.R. (N.S.W.) 172, 178 per Davidson J.

31 *Tramways Advertising Pty. Ltd.* v. *Luna Park (N.S.W.) Ltd.* (1938) 38 S.R. (N.S.W.) 632, 641 per Jordan C.J.; approved by the High Court in *Associated Newspapers Ltd.* v. *Bancks* (1951) 83 C.L.R. 322, 337.

32 [1962] 1 All E.R. 474. It was substantially repeated by Upjohn L.J. in *Astley Industrial Trust Ltd.* v. *Grimley* [1963] 2 All E.R. 33, and formed the basis of the criticism of 'fundamental breach' in the Opinion of Lord Upjohn in the *Suisse Atlantique* case, and in the judgment of Diplock L.J. in *Hardwick Game Farm* v. *Suffolk Agricultural and Poultry Producers Association Ltd.* [1966] 1 All E.R. 309, 346-347. See also *Ditchburn Equipment Ltd.* v. *Crich* (1966) 10 Sol. Jo. 266.

contract. However, Diplock and Upjohn L.JJ. went on in more general terms to propound that the question whether a breach of contract relieves the innocent party from further performance cannot be answered by classifying all contractual undertakings as conditions or warranties. The question has to be answered by looking at the event or circumstances to which the breach gives rise to determine whether it is such an event that it substantially deprives the innocent party of what he had contracted for and therefore relieves him of the obligation of further performance.[33] Applying this test to particular contracts, it may be found that breach of some terms can only give rise to events or consequences of this nature, and that these terms are therefore necessarily conditions (if there remains any point in 'tagging' them in this way). Breach of other terms, it may be postulated, can never give rise to such events, and these are therefore warranties. But there will remain a third category of terms in respect of which it is not possible to predict in advance whether a breach will or will not have this effect. It is therefore useless to attempt to classify these terms initially as conditions or warranties; one must wait upon the breach to determine whether or not it will have the effect of discharging the innocent party.

In the case of sale of goods and hire purchase, the condition/warranty dichotomy has a statutory basis, at any rate so far as the implied terms are concerned. But so far as express terms are concerned, and in general contractual undertakings governed by common law, the approach to these problems may well now be different if the reasoning of these cases is accepted.[34]

The Breakdown of the Consequences of the Classification

Not only has there in recent years been much reconsideration of the method of classifying affirmations and promises, but the whole point of the classification has tended to become blurred through an equation of the remedies. There seems to have been a recognition that 'rescission or nothing' is too drastic a response to many cases of innocent misrepresentation,[35] and that in the majority of cases the interests of the parties would be adequately protected by an award of damages which the orthodox approach forbids. This line of thought seems to underlie the recommendations of the (U.K.) Law Reform Committee 10th Report (1962) on Innocent Misrepresentation.[36] The Law Reform Committee recommended that damages should be available in lieu of rescission in

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33 Compare the doctrine of frustration which applies where this happens without breach of contract and therefore relieves both parties from further performance.

34 Compare *Uniform Commercial Code* (1962), Article 2 (Sales), which speaks generally of 'warranties' in the sense of 'terms', the questions of breach and remedies being separately dealt with in Parts 6 and 7 and not depending in any way upon an initial classification of the terms breached. See in particular *U.C.C.* s. 2-313.

35 In fact this feeling is probably reflected in the existence of the numerous bars to rescission for innocent misrepresentation, which make the remedy one that in practice is rarely available.

36 *Cmnd.* 1782.

the discretion of the court;[37] that if rescission were barred damages should still be awarded unless the representor were able to prove that at the time the contract was made he believed on reasonable grounds that the representation was true;[38] and that it should not be possible to exclude liability (whether in damages or rescission) for innocent misrepresentation unless the representor could show that up to the time the contract was made he had reasonable grounds for believing that the representation was true.[39]

The recommendations of this committee have recently been given effect in England by the Misrepresentation Act 1966, but that legislation had already been anticipated to some extent by the Master of the Rolls in his judgment in the *Dick Bentley* case.[40] Quite apart however, from these developments, other lines of authority had produced the position that it was no longer possible to accept without qualification the famous dictum of Lord Moulton that '. . . a person is not liable in damages for an innocent misrepresentation, no matter in what way or under what form the attack is made.'[41] The principle has in fact been outflanked, and the irony of the situation is that Lord Moulton himself in the same case pointed clearly the line of attack.

> It is evident, both on principle and on authority, that there may be a contract the consideration for which is the making of some other contract. 'If you will make such and such a contract I will give you one hundred pounds', is in every sense of the word a complete legal contract. It is collateral to the main contract, but each has an independent existence, and they do not differ in respect of their possessing to the full the character and status of a contract. . . . Such collateral contracts, the sole effect of which is to vary or add to the terms of the principle contract, are therefore viewed with suspicion by the law. They must be proved strictly. Not only the terms of such contracts but the existence of an *animus contrahendi* on the part of all the parties to them must be clearly shewn. Any laxity on these points would enable parties to escape from the full performance of the obligations of contracts unquestionably entered into by them, and more especially would have the effect of lessening the authority of written contracts by making it possible to vary them by suggesting the existence of verbal collateral agreements relating to the same subect-matter.[42]

A number of cases show that the result that Lord Moulton feared is exactly what has happened, and that it has happened because of the inadequacy of the 'rescission or nothing' rule. In fairness to Lord Moulton however, his dictum must be seen in its setting of 1912, when it was still more usual to see a warranty as an undertaking or assurance collateral to some other transaction such as a sale. With the newer use of 'warranty' to denote a minor term of a principal contract, confusion has crept in, and the way has been left open for giving contractual effect (on the basis of this notion of collateral contract) to statements which, for example, the parol evidence rule would keep out of the main

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37 *Ibid.*, paras. 11 and 12.

38 *Ibid.*, paras. 17 and 18.

39 *Ibid.*, paras. 23 and 24.

40 [1965] 2 All E.R. 65, discussed at p. 233 *supra*.

41 *Heilbut, Symons & Co.* v. *Buckleton* [1913] A.C. 30, 51.

42 *Ibid.*, 47. The doctrine of collateral contracts is of course considerably older than this. See cases cited by Wedderburn: *Collateral Contracts*, [1959] C.L.J. 58.

contract or which as part of the main contract would be caught by the Statute of Frauds. *De Lassalle* v. *Guildford*[43] is nicely illustrative of this confusion. It is frequently cited[44] as authority for the proposition that an oral assurance that the drains were in order was not a term of the lease but an independent collateral contract. In fact, a reading of the report shows that the Court held that there was only one contract, partly written and partly oral, and that the assurance was a term of the principal contract collateral to its main purpose.[45]

However, other cases have clearly used the 'two contract' concept to give contractual effect (and contractual remedies) to assurances that could otherwise have been held to be no more than mere representations.[46] In *City & Westminster Properties Ltd.* v. *Mudd*[47] there was a lease of premises as showrooms, workrooms, and offices only. Harman J. held that a prior oral assurance that the lessee would be allowed to sleep on the premises was part of a prior enforceable contract from which the lessor would not be permitted to resile. In *Webster* v. *Higgin*,[48] on the sale of a motor car, the seller's agent said to the buyer, 'if you buy the Hillman we will guarantee that it is in good condition.' The buyer then entered into a hire-purchase agreement with the seller which excluded all warranties, conditions, descriptions, and representations as to the vehicle. The Court of Appeal held that the seller was in breach of a separate contract prior to the hire-purchase agreement whereby the seller guaranteed the car in consideration of the buyer taking it on hire-purchase terms, and that this separate agreement was not caught by the wording of the exclusion clause in the hire-purchase agreement.

Australian cases have clearly recognized the doctrine of collateral contracts.[49] However, the Australian courts have been much more cautious than their English counterparts in its application. In *Shepperd* v. *Ryde Corporation*,[50] in which the High Court did find a collateral contract, Dixon, McTiernan, Fullagar, and Kitto JJ. issued a warning:

> The reluctance of courts to hold that collateral warranties or promises are given or made in consideration of the making of a contract is traditional. But a chief reason for this is that too often the collateral warranty put forward is one that you would expect to find its place naturally in the principal contract.

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43 [1901] 2 K.B. 215.

44 See Cheshire & Fifoot: *Law of Contract* (Aust. ed.) 203.

45 See Wedderburn: *loc. cit.* 66: 'The failure to observe the tautological nature of the parol evidence rule and to distinguish between the analyses of collateral term and collateral contract—(a failure usually occasioned by the fact that either analysis would equally well provide the answer desired by the court)—caused some judges great difficulty'. In origin a warranty was an assurance collateral to some other transaction such as a sale; hence the rule that breach of warranty did not affect the validity of the main transaction but sounded only in damages.

46 The 'tripartite' collateral contract cases, such as *Shanklin Pier Ltd.* v. *Detel Products Ltd.* [1951] 2 K.B. 854, and *Andrews* v. *Hopkinson* [1957] 1 Q.B. 229, are not relevant to this discussion.

47 [1958] 2 All E.R. 733.

48 [1948] 2 All E.R. 127.

49 See, for example, *Leipner* v. *McLean* (1909) 8 C.L.R. 306.

50 (1952) 85 C.L.R. 1, 13.

So the Australian courts appear to require clear proof of *animus contrahendi* in respect of the representation.[51] A collateral agreement will not be found if the court considers that the written contract was intended to embody the entire agreement between the parties.[52] In particular, the courts will not enforce a collateral agreement inconsistent with the terms of the main agreement and of which the effect would be to contradict the terms of a principal written agreement.[53]

A further, more conjectural, inroad into the rule that damages cannot be awarded for an innocent misrepresentation, lies in the application of the decision in *Hedley Byrne & Co. Ltd.* v. *Heller & Partners Ltd.*[54] The scope of the ratio of that decision is still much in doubt, but it does appear to translate the problem of liability in damages for negligent mis-statements from the province of contract to tort. The decision establishes the proposition that, in the absence of express disclaimer, a duty of care exists where information or advice is given in the course of professional or business affairs if a special relationship, based on the one side on skill and judgment, and on the other side on confidence and reliance, exists between the parties. The assumption of responsibility and the special relationship together give rise to the duty of care to make accurate statements. In the *Hedley Byrne* situation no contract came into existence between the respondents and appellants, but the appellants in reliance on the advice tendered by the respondents entered into other contracts which resulted in loss. However, if the statements of judicial opinion in this case are taken literally, it may not be unreasonable to suppose that this special relationship could exist between e.g. buyer and seller, at any rate where, because of the seller's superior knowledge and experience, it would be reasonable for the buyer to rely on the seller's assurances. If this is so, the buyer would have an action for damages if the representation were false, irrespective of whether or not the representation had been incorporated into the contract, but provided it had been made negligently.

Whether *Hedley Byrne* will be applied as between contracting parties is still not finally settled. There are so far only two reported cases in which this application has been suggested. In *Oleificio Zucchi S.P.A.* v. *Northern Sales, Ltd.*[55] McNair J., *obiter*, said '. . . as at

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51 *Clough* v. *Rowe* (1888) 14 V.L.R. 70. But how the question of *animus contrahendi* can ever really pass from conjecture to proof is difficult to see. In *Marsh* v. *Hunt Bros. (Sydney) Pty. Ltd.* [1958] S.R. (N.S.W.) 380, on the sale of a truck an oral assurance was given as to its age. Street C.J., at 384, found there was no *animus contrahendi*, the words used were 'not words of contract but words of representation'. From the report it would appear to have been just as easy to say the converse. The case does, however, illustrate the heavy onus that lies on the party seeking to set up a collateral agreement.

52 *Clough* v. *Rowe* (1888) 14 V.L.R. 70; *Cutts* v. *Buckley* (1933) 49 C.L.R. 189.

53 *Hoyt's Pty. Ltd.* v. *Spencer* (1919) 27 C.L.R. 133.

54 [1964] A.C. 465.

55 [1965] 2 Lloyd's Rep. 496, 519. A plea of collateral warranty also failed in this case.

present advised, I consider the submission advanced by the buyers, that the ruling in [*Hedley Byrne*] applies as between contracting parties, is without foundation'. In the New Zealand case of *Jones* v. *Still*[56] an attempt to raise *Hedley Byrne* between contracting parties also failed, but this time on the ground that the representation was as to a matter on which the representor 'might be expected to have knowledge, but it was not that specialist knowledge, equivalent to special skill, necessary to bring this case within the decision in *Hedley Byrne*, nor was he asked, even by implication, to exercise skill and judgment'.

The desirability of the extension of *Hedley Byrne* to representations between contracting parties may be open to some doubt. Where a contract results between the parties, a representor should be held liable for false representations, not on any principle of tortious fault or blame, but because in the contractual situation between the parties he must be taken to have assumed responsibility for the accuracy of his assurances. This assumption of responsibility is contractual in nature. It is part of the bargain between the parties. It should not be divorced from the contractual situation, and its scope and effect should be governed by the contract. The problem therefore is to make the law of contract sufficiently flexible to embrace the whole of the bargain between the parties, and to incorporate assurances of this nature within the scope of the contract, rather than to supplement the deficiencies of contract by extending notions of tortious fault liability. Even where no other contract results between those parties, the assumption of responsibility for the accuracy of a particular statement would, if the statement is acted upon, be more happily viewed within the context of contract than of tort.[57]

C. Excluding the Express Terms

The problem of finding the express terms of the contract, of ascertaining the true scope of the bargain between the parties, is not completed by a consideration of what the parties have said to one another. It is also necessary, in the light of modern methods of trading, to

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56 [1965] N.Z.L.R. 1071, 1074 per Wilson J.

57 See, for example, *Collen* v. *Wright* (1857) 8 E. & B. 647; *Colonial Bank of Australasia* v. *Cherry* (1867) 4 W.W. & A'B. 173 (affirmed by the Privy Council in L.R. 3 P.C. 24); *Starkey* v. *Bank of England* [1903] A.C. 114. And see discussion in Cheshire & Fifoot: *Law of Contract* (Aust. ed.) 146-148. Two particular difficulties stand in the way of this approach. The first is the problem of whether these cases can be extended beyond warranty of authority (See *Shanklin Pier Ltd.* v. *Detel Products Ltd.* [1951] 2 K.B. 854 in which none of these cases was cited). The second is that *Hedley Byrne* situations can be envisaged in which, if they are to be analyzed in terms of contract, the consideration for the assurance may be rather tenuous, insofar as it may be a matter of indifference to the representor whether or not his representations are acted upon. However, such cases could probably be satisfactorily disposed of on the ground of lack of intent to create legal relations.

consider the effect of statements and terms of the written contract which seek to limit the scope of the bargain by expressly excluding matters that might otherwise have given rise to additional express or implied terms—the problem of exclusion (or exemption or exception) clauses.

In approaching the problem of exclusion clauses, it is desirable at the outset to distinguish clearly between those clauses in contracts which seek to exclude implied terms and those that exclude express terms, because the policy considerations affecting these two types of clauses may well differ.

So far as implied terms are concerned, it is very much a question of policy as to how far it should be permissible to exclude them, involving in relation to sale of goods, for example, particular issues as to quality control and as to which persons in the distributive chain are best able economically to bear the risk of defective quality.[58] It may be that there is more general support today for the proposition that implied terms should no longer rest on the fictitious assent of the parties but, at any rate so far as quality control is concerned, should be requirements of law not excludable by the parties. This, however, is not pertinent to a discussion of the scope of the contract and the ability of the law to ascertain the true extent of the bargain.

The exclusion of express terms can, however, be viewed as an attempt by express provision in the contract to limit the area of contractual agreement. This, it is suggested, is unobjectionable to the extent that it seeks to define the true area of agreement as negotiated between the parties, but objectionable insofar as it arbitrarily and unilaterally curtails and limits the true understanding of the parties as it would otherwise have been found. Freedom of contract (which is rightly not an entirely discredited notion) postulates that the parties should be at liberty to determine by negotiation the precise extent of their contractual obligation, and to decline to accept liability in respect of casual unguarded statements or even of any statements other than those which have consciously and deliberately been reduced to writing. This seems a perfectly proper attitude provided there is neither surprise (in the sense of the deprivation from one party of a benefit which he had reasonable ground for thinking had been conceded to him) nor oppression.

The courts have avoided a direct frontal attack on exclusion clauses that might appear to have been made in circumstances rendering them

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58 Perhaps the least satisfactory feature of exclusion clauses is that they are found only where the opportunity for inserting them exists, namely where the transaction is at least in part effected by writing. So far as sales transactions are concerned, this means they may well be encountered at any stage in the distributive chain from manufacturer to consumer, except in the cash (as opposed to credit) sale at retail. This has two serious consequences. It means, first, that the retailer may well be saddled with legal responsibility for defective quality for which he is in no way to blame, simply because he has no opportunity to exclude or limit his liability in 'over the counter' sales, whereas all previous vendors in the chain may have incorporated exclusion clauses in their sales documentation. Secondly, in the absence of legislation, a distinction appears between the cash purchaser and the terms purchaser for which little justification is apparent.

'unconscionable', although in some jurisdictions there is statutory authority for the courts to disallow any term of certain types of contract on this ground.[59] Even in those jurisdictions, however, there seems to be some judicial reluctance to exercising such broad and ill-defined powers. Rather than launch a frontal attack, the courts have preferred to counter oppression and surprise by indirect means.

The first weapon in the armoury of the courts in this regard has been to seek to exclude the exclusion clause by a manipulation of the rules of offer and acceptance.[60] Hence it is established that, whilst an exclusion clause in a signed writing must necessarily stand part of the contract,[61] in other cases reasonable notice of the existence of the clause (or of printed conditions generally) must be given at or before the time of contracting. If, however, the clause clearly is contractual according to these rules, its effect may be limited by construction *contra proferentem.* Hence, the exclusion of express terms does not exclude implied terms, and vice versa, and the exclusion of conditions does not exclude warranties, and vice versa.[62] Similarly, any ambiguity in the scope of the clause will be construed against the party for whose benefit it was inserted.[63] Further, even though the exclusion clause appears wide enough to cover the matter of complaint, the court may hold that the clause was overridden by the conduct of the parties. This may be either because the effect of the exclusion has been misrepresented,[64] or because an express undertaking has been given which the court is prepared to hold supersedes the written denial.[65] Failing all else, the court must then construe the exclusion clause in its context in the whole of the contract to determine its scope and effect.[66]

It must now, no doubt, be taken as settled law that there is no absolute rule of law to the effect that an exclusion clause can in no circumstances exclude or limit liability for fundamental breach or breach of a fundamental term, but that the problem is simply one of determining as a matter of construction of the contract the effect of

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59 See *U.C.C.*, s. 2-302. Similar powers have existed in a number of jurisdictions in the earlier Hire-Purchase Acts and in the Moneylenders Acts, but, apart from striking at provisions stipulating excessive interest rates, little use appears to have been made of them.

60 See generally the 'ticket cases'.

61 *L'Estrange* v. *Graucob* [1934] 2 K.B. 394.

62 *Andrews Bros. (Bournemouth) Ltd.* v. *Singer & Co.* [1934] 1 K.B. 17; *Baldry* v. *Marshall* [1925] 1 K.B. 260; *Wallis, Son & Wells* v. *Pratt & Haynes* [1911] A.C. 394. This approach simply challenges those drafting exclusion clauses to produce the perfect clause.

63 *Szymonowski & Co* v. *Beck & Co.* [1923] 1 K.B. 457; *Alderslade* v. *Hendon Laundry Ltd.* [1945] K.B. 189.

64 *Curtis* v. *Chemical Cleaning and Dyeing Co.* [1951] 1 K.B. 805.

65 *Couchman* v. *Hill* [1947] K.B. 554; *Harling* v. *Eddy* [1951] 2 K.B. 739.

66 *Glynn* v. *Margetson & Co.* [1893] A.C. 351, 357 per Lord Halsbury L.C.: 'Looking at the whole of the instrument, and seeing what one must regard . . . as its main purpose, one must reject words, indeed whole provisions, if they are inconsistent with what one assumes to be the main purpose of the contract'.

the exclusion clause. A number of recent decisions have brought down the edifice of fundamental breach.[67]

It may be considered unfortunate that important principles of law are frequently expounded by highest appellate courts in the context of cases that are least appropriate for them. It is doubtful whether a less satisfactory fact situation could have been envisaged for a discussion of fundamental breach than the facts of the *Suisse Atlantique* case. In the first place, the parties in that case were at arms length, so that no question of surprise or oppression arose. Secondly, the particular clause under consideration was a demurrage clause which the House expressly held was not an exclusion clause; and the willingness of their Lordships to treat it as an exclusion clause, for the purpose of hanging on it a dissertation on fundamental breach, did not make it any more than a limitation clause (*i.e.* a clause recognizing the breach and limiting the damages recoverable), so that the whole discussion wears an air of artificiality and raises crucial questions as to the application of the dicta to exclusion clauses proper which deny any remedy at all or even that a breach has occurred. Finally, the innocent party was not seeking to terminate the contract, but had affirmed it with knowledge of the breach, and alleged simply that damages were not controlled in the events that had occurred by the demurrage clause but were at large. In the result it is feared that considerable difficulty may yet be encountered in working out the method of construction of exclusion clauses.

It may well be, for instance, that it cannot be taken as settled that, although there is no rule of law automatically striking out exclusion clauses in the event of fundamental breach or breach of a fundamental term, nevertheless it is no longer necessary to enquire whether a particular term or a particular breach is fundamental. Lord Upjohn, in his Opinion,[68] clearly recognizes the continued existence of a notion of 'fundamental term' distinct from 'fundamental breach'. He defined 'fundamental breach' as a mere

> convenient shorthand expression for saying that a particular breach or breaches of contract by one party is or are such as to go to the root of the contract which entitles the other party to treat such breach or breaches as a repudiation of the whole contract. Whether such breach or breaches do constitute a fundamental breach depends on the construction of the contract and on all the facts and circumstances of the case.

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67 They are, in the Court of Appeal, *U.G.S. Finance Ltd.* v. *National Mortgage Bank of Greece* [1964] 1 Lloyd's Rep. 446, 453 per Pearson L.J. (cp. Lord Denning M.R. at 450), and *Hardwick Game Farm* v. *Suffolk Agricultural and Poultry Producers Association Ltd.* [1966] 1 All E.R. 309 (the 'SAPPA' case); in the House of Lords, *Suisse Atlantique Societe D'Armement Maritime S.A.* v. *N.V. Rotterdamsche Kolen Centrale* [1966] 2 W.L.R. 944; and in the High Court of Australia, *Council of the City of Sydney* v. *West* (1965) 39 A.L.J.R. 323.

68 [1966] 2 W.L.R. 944, 978-979. See also per Viscount Dilhorne at 953-955, and Lord Hodson at 970. Lord Reid and Lord Wilberforce did not consider the question of fundamental term distinct from fundamental breach. To Lord Upjohn's example of fundamental breach, the rest of the House added two more categories: (i) a performance totally different from that contemplated by the contract, and (ii) repudiatory conduct evincing an intention no longer to be bound.

'Fundamental term' he defined as

> a stipulation which the parties have agreed either expressly or by necessary implication or which the general law regards as a condition which goes to the root of the contract so that *any* breach of that term may at once and without further reference to the facts and circumstances be regarded by the innnocent party as a fundamental breach and thus is conferred on him the alternative remedies at his option that I have just mentioned [of treating the whole contract at an end (including any exception clause) and suing for damages generally, or of affirming the contract and treating it as continuing on foot in which case his right to damages is governed by the contract including the exception clause, subject to construction of that clause *contra proferentem*].

In His Lordship's view, therefore, it follows from the ordinary rules of contract that, wherever there is a fundamental breach or a breach of a fundamental term which is accepted by the innocent party as repudiation, the contract is at an end and the guilty party can no longer rely on any special exemption provided by the contract. If this analysis is accepted then it will still remain necessary to enquire whether particular terms are to be regarded as fundamental.

However, Lord Upjohn's definition of 'fundamental term' would serve equally well as a definition of a 'condition' of the contract as contrasted with 'warranty.'[69] Hence, it may be necessary to enquire whether a term is fundamental only in those cases in which the condition/warranty dichotomy is not statutory, and which instead may be governed by the new approach to breach first enunciated by Lord Upjohn, amongst others, in the *Hong Kong Fir* case.[70] In other words, where it is not necessary to enquire whether a term is a condition or warranty, but instead to determine the rights of the innocent party from an examination of the consequences of the breach, it may nevertheless be that by express agreement, necessary implication, or general law, any breaches of particular terms may have to be taken as a repudiation of the contract if the innocent party elects to treat them as such. It seems to matter little whether or not one chooses to call such terms 'fundamental'. Similarly, the various examples of 'fundamental breach' that appear in the Opinions represent no more than a classification of the types of breach that according to ordinary existing principles may discharge the contract, and it serves little purpose to tag them as 'fundamental'.

A more serious difficulty with Lord Upjohn's analysis concerns the proposition that

> it is the consequence of the application of the ordinary rules applicable to all contracts, that if there is a fundamental breach accepted by the innocent party the contract is at an end; the guilty party cannot rely on any special terms in the contract.[71]

If this is now to be taken as the law it would appear to be a new departure, for whilst a contract is undoubtedly discharged for the future once the breach is accepted by the innocent party as a repudia-

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69 See *Behn* v. *Burness* (1863) 3 B. & S. 751, 755, and Sale of Goods Act 1896 (Tas.), s. 16(2).

70 [1962] 2 Q.B. 26, discussed at p. 234 *supra.*

71 [1966] 2 W.L.R. 944, 982. See also per Lord Reid at 958.

tion, nevertheless it appears always to have been settled that the discharge does not operate retrospectively. The contract, including the exclusion clause, should continue to govern performance up to and including the time of breach (or even of the acceptance of the repudiation) and would therefore control the questions whether there has in fact been a breach and what if any remedy the parties must be taken to have agreed should lie for it.[72]

It is submitted with respect that, whilst the insistence that the effect of exclusion clauses is a matter of construction for the court is to be welcomed, the approach to the constructional problem propounded in general terms in *Suisse Atlantique* represents a considerable over-simplification of the problem. Not all exclusion clauses are concerned, as was the one in *Suisse Atlantique*, simply to limit the damages recoverable. They appear in many guises and seek to achieve their purpose in many ways. They may exclude all remedy for what is acknowledged would be a breach, or they may even negative the occurrence of a breach as by limiting or excluding what is or would otherwise be a term of the contract. The terms of exclusion are as much part of the contract as any other terms, and in particular the question whether a certain term is to be regarded as 'fundamental' may well not be answerable except by reference to the exclusion clause which helps to define the scope and extent of the obligation under the contract. The primary question for the court in all cases is 'What have the parties contracted for?—What is the scope of the bargain?' All the clauses of the contract go to defining this—it is the whole object of 'warranty'. Therefore both clauses creating 'warranties' and those seeking to exclude them are relevant. It is an over-simplification to say that a man does not perform a contract to sell peas by delivering beans; a construction of the whole contract may show that the parties have agreed that the seller should be permitted to discharge his obligation by delivering either peas or beans at his option. The question whether this sort of construction should be open to the court is peculiarly one of economic policy in the field of consumer protection.[73]

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72 Amongst a wealth of authority on this point, see for example *Heyman* v. *Darwins Ltd.* [1942] A.C. 356. Lord Macmillan, at 374, said: 'The contract is not put out of existence, though all further performance of the obligations undertaken by each party in favour of the other may cease. It survives for the purpose of measuring the claims arising out of the breach, and the arbitration clause survives for determining the mode of their settlement. The purposes of the contract have failed, but the arbitration clause is not one of the purposes of the contract'. There seems no ground for distinguishing in this matter between arbitration and exclusion clauses. Lord Porter, at 397, said: 'The injured party may sue on the contract forthwith whether the time for performance is due or not . . . he is still acting under the contract. He requires to refer to its terms at least to ascertain the damage, and he may require to refer to them also if the repudiation of the contract is in issue'.

73 Lord Reid, at 965, foresaw that this purification of the law of contract might produce economic problems, but, with the knowledge that the matter figured on the agenda of the Law Commission, was able merely to point to the 'need for urgent legislative action' with some measure of confidence. If Australia is to inherit the decision, one can only hope that it will not be too long before legislative action follows here also, preferably on a uniform basis.

It is therefore suggested that there is no longer any point in continuing to enquire whether a term or a breach should be regarded as 'fundamental', and that these expressions should be allowed to pass out of the law. It should today be simply a question of construction, first whether the parties have agreed that any breaches of certain terms should discharge the contract, and secondly whether in other cases particular breaches do discharge the contract. It is submitted that the whole problem was analysed most clearly in the judgment of Diplock L.J. in the *SAPPA* case.[74]

> . . . the so-called 'doctrine of fundamental breach' is no more than a rule of construction based on the presumed intention of the contracting parties; that is, as ascertained by determining what each party by his words and acts reasonably led the other party to believe were the acts which he was undertaking a legal liability to perform. Just as there are some original rights and liabilities which arise by implication of law from the nature of the contract itself, there are also substituted rights which a party acquires by implication of law when the other party fails to perform an act which he undertook a legal obligation to perform, or performs an act which he undertook not to perform. Such substituted rights depend on the nature of the event to which that act or omission gives rise: see *Hong Kong Fir Shipping Co. Ltd.* v. *Kawasaki Kisen Kaisha Ltd.* It may be a mere right to recover monetary compensation for the non-performance, that is damages, or, in addition, to be relieved from any obligation further to perform any acts which he, for his part, had undertaken a legal obligation to perform, or, in addition, to recover from the other party any money or other valuable consideration which he had previously paid or transferred to such other party. Just as the original rights and liabilities which arise by implication of law from the nature of the contract itself can be negatived or modified if this can be demonstrated to be the presumed intention of the parties, so can such substituted rights.
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> The expression 'exemption clause' is loosely used to include both clauses in contracts which negative or modify what I have called above original rights and liabilities which arise by implication of law from the nature of the contract itself and also clauses in contracts which negative or modify those substituted rights which a party acquires by implication of law on failure by the other party to perform an original liability; but the basic rule of construction applicable to both kinds of exemption is the same. When, in relation to the subject-matter of a contract, an event occurs as a result of an act or omission of a party to the contract which is alleged to entitle the other party to a legal remedy, the first task of the court is to look at the event and to ascertain what the presumed intention of the parties was as to what should be their legal rights and liabilities on the occurrence of an event of that kind. At the one extreme the event may be the result of an act so different from any act which the party by his contract undertook any legal liability to perform, that the event cannot be said to be one contemplated under the contract at all. Independently of the contract it may give rise to liabilities in tort, for example for conversion or negligence, and may be accompanied by a failure to perform an act which the party undertook by his contract to perform which gives rise to a secondary right of the other party under the contract itself . . .
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> When applied to this kind of event the expression 'fundamental breach' means a total failure by one party to perform a contract of the kind into which he has entered. So far as it appears from the words and conduct of the parties that they intended to enter into a contract of that kind an exemption clause cannot be drafted in wide enough terms to cover this kind of event without either destroying the contract altogether or changing its character. If it is wide enough to exempt one party from performance while binding the other party to perform it, the contract is either void for lack of consideration or transformed from a bilateral synallagmatic contract into a unilateral or 'if' contract

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74 *Hardwick Game Farm* v. *Suffolk Agricultural & Poultry Producers Association Ltd.* [1966] 1 All E.R. 309, 346-347.

> in which one party undertakes a legal liability to perform acts if the other party performs other acts but the other party undertakes no legal liability to perform such other acts. It would, I think, be conducive to clarity in the law of contract if the expression 'fundamental breach' were restricted to events of this kind, but in recent years it has been applied by this court to a much wider class of events than this. I doubt if it has any more precise meaning than an event which is not dealt with in the particular exemption clause relied on in the particular contract under consideration by the court, and accordingly has such consequences as would arise by implication of law on the happening of an event of that kind under a contract of the character under consideration. But whether the plaintiff chooses to call the event which he alleges gives him a substituted right against the defendant, a breach of warranty, a breach of condition, or a fundamental breach, the task of the court is the same: to look at the event, and to ascertain from the words and conduct of the parties which created the contract between them what their presumed intention was as to what should be their legal rights and liabilities either original or substituted on the occurrence of an event of that kind.

D. Proposals for Reform

The process described in the preceding pages is the process which the courts have to follow or appear to follow in ascertaining the scope of the contract. It is suggested that this process is manifestly absurd, and that, whilst no process of construction can be reduced to simple rules of thumb, a great deal can be done to clear the dead wood, close the blind alleys, and release the courts from many of the devices which may have to be employed to do substantial justice in any particular case. It is for this reason that the demise of 'fundamental breach' is welcomed, although its absence will leave a serious gap in the armoury of the courts unless flexibility can be introduced into the whole of this area. The object of any reform should be to sweep away archaic rules and distinctions that have no foundation in principle, and concepts that have outworn their usefulness, and to liberate the courts to ascertain (still by the application of objective standards) the scope of the real bargain between the parties without having to resort to the devious techniques that confuse and disfigure modern law.

As a starting point it is submitted that there is a complete lack of legal principle or any policy justification behind the present classification of statements as mere representations or contractual terms. The classic test of intention is unrealistic, first because it is unlikely that the parties ever formed or expressed any clear intention on the matter, and secondly because, as has been demonstrated above, that test tends in practice to give way to various ancillary tests even though the courts may continue to pay lip-service to orthodox doctrine. Furthermore, it is no more realistic to seek to justify the classification on the ground that mere representations relate to minor inducements to contract whereas warranty relates to more important considerations. It may be seriously challenged whether this is necessarily so, and in any event the argument would rest on a false premise that rescission of the whole contract for innocent misrepresentation is a less drastic remedy than an adjustment of the consideration by way of damages.[75] It may well be

[75] See Law Reform Committee, 10th Report (1962), *Cmnd.* 1782, para. 11.

that the existence of so many bars to rescission for innocent misrepresentation means that rescission can rarely be granted in such cases, but the withholding of all remedies where the rights of the parties could be satisfactorily adjusted by an award of damages scarcely seems justifiable. The argument that contractual remedies should not be given for matters of minor importance—*i.e.* matters which the parties have not considered of sufficient importance to put into their contract—is misleading. It begs first of all the question how it is to be determined whether or not they have put them in their contract, and secondly the question as to what we mean by 'contractual remedies'. There are in fact substantially only two contractual remedies,[76] rescission and damages. Any argument based on a distinction between rescission for matters in the formation of the contract and rescission for breach breaks down because most terms may well start life as mere representations—there is no distinction in principle between the two. It is submitted that if a statement induced the making of the contract, it is part of the bargain between the parties and should be viewed as contractual. The question of the appropriate remedy if the statement should turn out to be untrue is a separate issue that should not be allowed to obscure the problem of ascertaining the extent of the true agreement.

The notion that a representation may induce a contract and yet not form part of that contract, is not the result of any reasoned policy decision, but appears to be the accidental product of the interaction of several factors. The major factor is undoubtedly the parol evidence rule, whereby, if the court considers that the writing is intended by the parties to contain the entire agreement between them, neither party may adduce oral evidence to add to, vary or contradict the writing or to show that the writing misstates his intention.[77] Where the rule is applied by the court, then any oral statement can be pleaded only as an innocent misrepresentation,[78] *i.e.* as a ground in equity for setting aside the transaction. Even the equitable remedy of rectification may, in certain circumstances, be excluded by this rule. In *Rose* v. *Pim*[79] the buyer, relying on the seller's assurance that horsebeans and feveroles were the same thing, orally agreed to buy horsebeans and this oral agreement was later reduced to writing. A sub-buyer subsequently claimed damages from the buyer on the ground that he had requested feveroles and horsebeans did not answer that description, and the buyer sought to pass back the claim for damages to the seller. He was faced with the difficulty that to found a claim for damages the statement that horsebeans and feveroles are the same thing would have to be shown to be contractual. As the contract had been reduced to writing,

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76 Ignoring specific performance and injunction as not being relevant to this discussion.

77 See the discussion of this rule in Wedderburn: *Collateral Contracts*, [1959] C.L.J. 58, 59-64.

78 Ignoring for the moment the possibility that the statement might be pleaded as a separate collateral contract.

79 [1953] 2 Q.B. 450.

the only way this could be done would be by rectifying the writing to read 'feveroles' instead of 'horsebeans'. The Court of Appeal held that rectification could not be granted. The oral agreement was for horsebeans and the writing correctly stated this.

> There was, no doubt, an erroneous assumption underlying the contract — an assumption for which it might have been set aside on the ground of misrepresentation or mistake — but that is very different from an erroneous expression of the contract, such as to give rise to rectification.[80]

It is submitted that a law of contract that cannot construe the facts in this case as giving rise to an agreement to buy and sell feveroles is defective. The whole basis on which the parties contracted was the seller's assurance that horsebeans and feveroles were the same thing, and the law needs to be flexible enough to embrace such an assurance within the scope of the contract. If the underlying assumption of the contract is not to be treated as contractual, it is small consolation to say that nevertheless treated as an innocent misrepresentation it might have justified setting the contract aside—a course which in the event was not open to the parties.

The difficulty with the parol evidence rule today is that it has been so undermined with exceptions that it is now little more than a presumption—'namely that a document which *looks* like a contract is to be treated as the *whole* contract'.[81] Accordingly, the answer to the question whether the court considers that the writing is intended to represent the entire agreement, may well depend on the weight it is prepared to attach to oral statements made during negotiations. The process, therefore, is completely circular. Furthermore, even if the court is prepared to apply the rule to exclude evidence of a parol statement as a term of the contract, it may in the next breath side-step the rule by allowing the statement to be proved as a term of a collateral contract not inconsistent with the main contract. So in *Rose* v. *Pim*, Denning L.J., after the passage cited above, continued:

> There is one other matter I must mention. In the statement of claim the plaintiffs originally claimed damages for breach of a collateral warranty — a warranty that the horsebeans would be a compliance with a demand for 'feveroles'— but that claim was formally abandoned at the trial. I do not myself quite see why it was abandoned. Section 4 of the Sale of Goods Act 1893 was no bar to it. Nor was such a warranty in any way in contradiction of the written contract. . . . The only difficulty in such a claim might be whether there was a contractual warranty or merely an innocent misrepresentation. I should myself have thought that it had a better chance of success than the claim for rectification.[82]

Other factors that have helped to produce a separate category of innocent misrepresentation are, first, the requirements of writing (or of written evidence) for certain types of contract, which not merely bring into play the parol evidence rule, but also mean that if further oral terms are admitted there may be no contract at all or only an unenforceable

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80 *Ibid.*, 462 per Denning L.J.

81 Wedderburn: *loc. cit.*, 62.

82 [1953] 2 Q.B. 450, 462-463.

one.[83] However, the occasions for writing have been steadily reduced in many jurisdictions in recent years, and the major reason for the requirement of writing (the inability of the parties to the contract to give evidence of its terms) no longer exists. Yet innocent misrepresentation persists. The final factor, it is suggested, is the historic division between common law and equity jurisdiction, whereby the normal common law remedy was damages (and only very occasionally, and in a limited form, rescission); whilst in equity, although damages could not be awarded, a contract might be set aside, as long as rescission was practicable, on account of matters which the common law would not construe as breaches of the terms of the contract.

The proposals of the English Law Reform Committee on Innocent Misrepresentation,[84] whilst they would undoubtedly go a long way towards ameliorating the position, are open to criticism on the ground that they do not go far enough. They appear to tinker with and to patch up a thoroughly unsatisfactory area of the law without coming to grips with the real problems. By largely equating the remedies for the various categories of affirmations, but leaving the categories intact, they may well only further confuse the law. If rescission or damages are to be alternative remedies, in the discretion of the court, for all false affirmations, then there appears to be little point in retaining innocent misrepresentation as a separate category.

The absence of justification for the retention of the separate category of innocent misrepresentation is the first major submission of this paper. The second is that the question of remedies for breach should not be allowed to confuse the search for the true scope of the contract, but should be viewed as a quite separate issue. It is submitted that the question of what remedies should be available for false affirmations or promises should turn, not on an initial arbitrary classification of the affirmation or promise, but on the nature of the consequences that flow from the breach. The distinction in this regard between conditions and warranties serves little useful purpose and should disappear from the law. An affirmation or promise, if it has any legal effect, should be regarded simply as a term of the contract, and the rights of the parties on breach should depend on a proper construction of the contract in the light of the circumstances that actually result from the particular breach.[85]

E. Conclusions

1. Any statement made in the course of negotiations which becomes part of the basis of the bargain,[86] in the sense that its natural tendency would be to induce the other party to enter into the contract, should

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83 Unless the oral term is held to be part of a separate collateral contract.

84 Discussed at p. 235 *supra.*

85 This is the approach taken in the *Hong Kong Fir* case and other cases cited in note 32 *supra.* For clarity, it might well be confirmed in codifying legislation.

86 *Cf. U.C.C.*, s. 2-313.

be a term of the contract. The facts of inducement and reliance make it part of the area of contractual understanding, and indicate an assumption of responsibility for its accuracy.

To implement this proposal it would be necessary that innocent misrepresentation should disappear from the law. A statement would have either contractual effect or no effect whatsoever, depending on whether or not inducement and reliance were present, and there would be no room for the application of either the *Hedley Byrne* decision[87] or the doctrine of collateral contracts if a contract in fact resulted between the parties. This would go a long way towards adopting the test propounded by Lord Denning in the *Dick Bentley* case,[88] except that it would reject the reversion to innocent misrepresentation where the representor was innocent of fault. The question whether a statement is contractual or not should be determined objectively, and contractual effect should not be denied to a statement because of the subjective beliefs or innocence of the maker. It is submitted that a statement is contractual if the representor has assumed responsibiliy for its accuracy — otherwise it is nothing — and the innnocence or fault of the representor are irrelevant. A further consequence of the proposal would be that artificial distinctions between representations of fact, law, opinion, and intention would disappear. Whatever the nature of the representation, if responsibility is assumed for its accuracy, it is contractual; and if it is a representation of intention that is caught up in the contract, it is then within the consideration and becomes an actionable promise. This might incidentally reduce the number of occasions on which a plea of 'mistake' might be raised.

The implementation of this proposal would also require some modification and clarification of the parol evidence rule. As a broad general proposition, where a contract is oral, all antecedent points of agreement prior to the culmination of negotiations are properly part of the contract. Where a contract is written, all antecedent points of agreement should ideally be recapitulated in the writing. However, this is in fact rarely done (for fairly obvious practical reasons) except in fairly rare and important cases. For example, in negotiations for the sale of a house, the vendor may well undertake to the purchaser to repair the spouting, but it is quite possible that this undertaking would not be incorporated in the written contract of sale if only because the parties forget to tell their solicitors about it. Nevertheless it is properly viewed as part of the contract between the parties, and it should be possible to achieve this result without engaging in casuistry under the parol evidence rule or resorting to the unpredictable doctrine of collateral contracts.

2. It should remain possible for the writing to exclude a statement which the court would otherwise be prepared to hold, applying the

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87 [1964] A.C. 465.

88 [1965] 2 All E.R. 65, discussed at p. 233 *supra*.

test described above, had become an express term of the contract. It is still important that the parties retain the liberty to insist that the whole measure of their obligations and liabilities should be gauged by the writing and by nothing else. However, statements in the writing that the writing is the whole contract, or denying that other representations or promises were made, or that such other representations or promises induced the contract, should not of themselves have contractual effect. Instead they should be regarded as merely evidentiary, to be taken into account by the court in deciding as a question of fact what was said and whether it operated as an inducement to contract. Greater weight would of course be attached to such a purported exclusion in a specially negotiated written contract than in a standard form printed agreement or a contract of adhesion.

By contrast, it may be considered that no objection could be taken to a clause of the contract which recognized the existence of other terms but which in some way limited or provided alternative remedies for breach, as long as the limitation or alternative remedy did not amount to a substantial deprivation of any remedy for the breach. The scope and effect of the purported limitation would be a matter for construction by the court in the light of the circumstances arising from the breach.

3. The present dichotomy between warranties and conditions should disappear, so that no distinction would be drawn between the various terms of a contract (except by the parties themselves). Whether a breach discharges the contract or merely gives rise to an action for damages is therefore a matter of construction for the court in the light of the consequences of the breach. However, it is suggested that in relation to sale of goods and hire-purchase, where knowledge and certainty as to rights are of prime importance and frequently cannot afford to wait upon a judicial determination, the buyer should in every case have the option of either rejecting the goods or of claiming damages, unless the contract itself limits his remedy or provides some alternative remedy.[89]

Apart from this particular instance in sale of goods, it is submitted that certainty, in the sense of rigidity and lack of flexibility, is not the primary object that should be pursued by any reforming legislation. It is always important that the parties should know their rights, but the process of discovery should be a realistic one. It is submitted that the process of ascertaining the scope of the contract is essentially a process of construction in which rules of thumb can only work unjustly, and flexibility should be the keynote. The present law is far from certain in its application. Tests of intention, the parol evidence rule, the doctrine of collateral contracts, etc. are merely unpredictable tools that the courts may juggle to achieve a just result, and they merely conceal that already the courts exercise a very broad discretion in ascertaining

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89 *Cf. U.C.C.*, s. 2-601.

the contract. The object of the reform herein proposed is to clear the dead-wood and to enable the courts to approach their task with an untrammeled recognition that their object is to ascertain 'What have these parties agreed upon?' That is the first purpose of the Law of Contract.