RECENT DEVELOPMENTS IN THE LAW OF CONTRACTS†

*Emil J. Hayek**

† Revised version of a paper presented at the "Continuing Legal Education Programme" held at the Faculty of Law, Common Law Section, University of Ottawa, Oct. 21-22, 1983.

* Faculty of Law, University of Ottawa.

I. THE CONSTRUCTION OF CONTRACTS

A. *Uncertainty*

> In the daily practice of the law, the most important subject is the construction of documents. Yet it is the subject on which opinions are still much divided. There are the "strict constructionists" on the one hand: and the "intention" seekers on the other hand. The strict constructionists go by the letter of the document. The "intention" seekers go by the purpose or intent of the makers of it.[1]

Although words are the tools of the lawyer's trade, they may nevertheless fail, sometimes because of imprecision in the words themselves. This is particularly so when we are concerned with documents drafted by non-lawyers. Lord Wright commented that "[b]usiness men often record the most important agreements in crude and summary fashion; modes of expression sufficient and clear to them in the course of their business may appear to those unfamiliar with the business far from complete or precise."[2] It is therefore not surprising that courts are frequently called upon to construe documents which are uncertain or ambiguous.[3] It has been stated that the function of the courts is to construe the contract without constructing it.[4] In the leading Canadian case of *Murphy v. McSorley*, Mignault J. stated that "[t]he court cannot make for the parties a bargain which they themselves did not make in proper time."[5] A similar approach was used by the House of Lords in *May & Butcher Ltd. v. The King*.[6] This strict, constructionist approach was subsequently relaxed in the often-quoted judgment of the House of Lords in *Hillas & Co. v. Arcos Ltd.*,[7] which was referred to and applied by the Court of Appeal in *Foley v. Classique Coaches Ltd.*,[8] and the House of Lords in *Scammell & Nephew Ltd. v. Ouston*.[9] In *Hillas & Co. v. Arcos Ltd.* Lord Wright stated, "It is, accordingly, the duty of the court to construe such documents fairly and broadly, without being too astute or subtle in finding defects, but, on the contrary, the court should seek to apply the old maxim of English law, *verba ita sunt intelligenda*

---

[1] A. DENNING, THE DISCIPLINE OF LAW 4 (1979).

[2] Hillas & Co. v. Arcos Ltd., [1932] All E.R. 494, at 503, 147 L.T. 503, at 514 (H.L.).

[3] *See* Scrimes v. Nickle, [1982] 1 W.W.R. 653, 130 D.L.R. (3d) 698 (Alta. C.A.), *leave to appeal to S.C.C. denied* 35 A.R. 180, 41 N.R. 572 (1982); G.S.B. Devs. Ltd. v. Chiulli, 15 B.C.L.R. 381 (S.C. 1979), *aff'd* 28 B.C.L.R. 157 (C.A. 1981), *leave to appeal to S.C.C. denied* 38 N.R. 380 (1981); Western Log Exch. Ltd. v. Soucie Constr. Ltd., 14 B.C.L.R. 293, 8 Bus. L.R. 1 (S.C. 1979), *aff'd* 21 B.C.L.R. 57 (C.A. 1980); First City Invs. Ltd. v. Fraser Arms Hotel Ltd., [1979] 6 W.W.R. 125, 104 D.L.R. (3d) 617 (B.C.C.A.); Adam v. General Paper Co., 19 O.R. (2d) 574, 85 D.L.R. (3d) 736 (H.C. 1978); Anderson v. Chaba, 7 A.R. 469, 81 D.L.R. (3d) 449 (C.A. 1977).

[4] Fridman, *Construing, Without Constructing, a Contract*, 76 L.Q.R. 521 (1960).

[5] [1929] S.C.R. 542, at 546, [1929] 4 D.L.R. 247, at 250.

[6] [1934] 2 K.B. 17, 103 L.J.K.B. 556 (H.L. 1929).

[7] *Supra* note 2.

[8] [1934] 2 K.B. 1, 103 L.J.K.B. 550 (C.A.).

[9] [1941] A.C. 251, [1941] 1 All E.R. 14 (H.L. 1940).

ut res magis valeat quam pereat."[10] This approach is based on the intent of the parties rather than on the strict construction of the document, and has been generally followed in subsequent cases both in England and Canada.

In the recent decision of the Ontario Court of Appeal in *Canada Square Corp. v. VS Services Ltd.*,[11] Mr. Justice Morden not only reaffirmed this principle but adopted a liberal and pragmatic approach to the requirement of certainty.

The representatives of Canada Square Corporation and VS Services Ltd. began discussions during the summer of 1969 about the establishment of a restaurant to be run by VS Services in a building to be built by Canada Square. At that time the building was at the drawing stage and if there was to be a restaurant at the top of the building, it was important that it be planned in the early stages. In October 1969, a document was drafted and signed by VS Services which read: "This is to confirm our verbal understanding of this morning regarding the restaurant. . . which is to become a part of Canada Square. . . ."[12]

There followed fourteen paragraphs stating the points discussed. The document ended, "This constitutes the general principles of our agreement with you."[13] Canada Square accepted the agreement and until May 1971 both parties acted as though they were contractually bound by the agreement. Eventually VS Services backed out of the agreement because of its lack of financial capability and Canada Square sued for the breach of contract. At the trial[14] VS Services was found liable and appealed. The main issue was whether the document, signed by both parties, constituted a concluded and enforceable agreement. The appellant's main contention was that the document of October 1969 did not represent a concluded contract, that the parties were negotiating subject to contract and that in any event the terms were so uncertain and impossible of performance as to be unenforceable. It is obvious that the language of the document was vague and crude and that many matters were not dealt with. The document itself states that it is "a verbal understanding of this morning regarding the restaurant", the body of the document was prefaced as "points discussed" and the document closed with, "[t]his constitutes the general principles." Notwithstanding this language, Morden J.A. found, in a well-written and reasoned judgment, that there was a concluded contract.

Dealing first with the contention that the document of 14 October did not represent a concluded contract, but rather an agreement which was "subject to contract", and, accordingly no contract at all, Morden J.A. adopted a common sense approach. He stated that it was important to consider "the genesis and aim of the transaction",[15] and observed that

[10] *Supra* note 2.

[11] 34 O.R. (2d) 250, 130 D.L.R. (3d) 205 (C.A. 1981).

[12] *Id.* at 253, 130 D.L.R. (3d) at 209.

[13] *Id.* at 255, 130 D.L.R. (3d) at 210.

[14] Canada Square Corp. v. VS Servs. Ltd., 25 O.R. (2d) 591, 101 D.L.R. (3d) 742 (H.C. 1979).

[15] *Supra* note 11, at 260, 130 D.L.R. (3d) at 215.

it was in the mutual interest of the parties to settle the matter, in a final way, as early as possible. The restaurant project could not go forward in any realistic way without the parties being contractually bound to each other and an agreement to agree would not have been realistic in this context. Furthermore, following 14 October, the parties by their words and actions conducted themselves in a way which indicated that they considered they had a binding contract.[16] Although the case is not referred to, this reasoning is reminiscent of that in *Foley v. Classique Coaches Ltd.*,[17] where Scrutton L.J. held that there was a valid contract because the parties believed they had a contract and acted for three years as if they had one.[18]

Having thus found an intent to make a contract, Morden J.A. dealt with the alleged uncertainty. He quoted passages from *Hillas & Co. v. Arcos Ltd.*[19] and *Scammell & Nephew Ltd. v. Ouston*[20] and concluded by paraphrasing Lord Wright's *dicta* in *Hillas & Co. v. Arcos Ltd.*:

> In this case there is no doubt that the document of October 14, 1969, as an agreement to lease, is crudely expressed and contains some very loose language. Further, a more sophisticated document would probably have covered several other matters in addition to those dealt with in it. Nonetheless, accepting that the parties intended to create a binding relationship and were represented by experienced businessmen who had full authority to represent their respective companies, a court should not be too astute to hold that there is not that degree of certainty in any of its essential terms which is the requirement of a binding contract.[21]

B. *Contracts of Indefinite Duration*

Contracts are sometimes entered into which are either silent as to their duration or contain phrases indicating they could continue in perpetuity. Problems arise when, due to changed conditions, particularly inflation, such contracts become too onerous and the disadvantaged party seeks to terminate them.

Two such contracts of indefinite duration were considered recently by the English Court of Appeal and the Ontario Court of Appeal respectively. The cases were based on similar factual situations but the judgments delivered were diametrically opposed.

In *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.*,[22] an agreement was entered into in 1929 for the supply of water "at all times hereafter" at a fixed rate. Fifty years later the normal rate was more than six times the agreed fixed rate and the water supply

---

[16] *Id.* at 260–61, 130 D.L.R. (3d) at 216–17.

[17] *Supra* note 8.

[18] *Id.* at 10, 103 L.J.K.B. at 553.

[19] *Supra* note 2.

[20] *Supra* note 9.

[21] *Supra* note 11, at 262, 130 D.L.R. (3d) at 218.

[22] [1978] 3 All E.R. 769, [1978] 1 W.L.R. 1387 (C.A.), *leave to appeal denied* [1979] 1 W.L.R. 203 (H.L.).

company purported to terminate the contract on six months notice. On appeal it was held that the contract was terminable on reasonable notice, even though the contract itself contained no provisions for termination by notice and contained the words "at all times hereafter." Two members of the English Court of Appeal held that it was the intention of the parties, gathered from all the circumstances, that the contract was terminable by reasonable notice.

Lord Denning arrived at the same result but by altogether different reasoning:

> [T]he rule of strict construction is now quite out of date. It has been supplanted by the rule that written instruments are to be construed in relation to the circumstances as they were known to or contemplated by the parties; and that even the plainest words may fall to be modified if events occur which the parties never had in mind and in which they cannot have intended the agreement to operate.[23]

He stated further that "[i]f events occur for which [the parties] have made no provision, and which were outside the realm of their speculations altogether then the court itself must take a hand and hold that the contract ceases to bind."[24] In His Lordship's opinion agreements in perpetuity are unequal. He noted that costs go "up with inflation through the rooftops: and the fixed payment goes down to the bottom of the well. . . . Rather than tolerate such inequality, the courts will construe the contract so as to hold that it is determinable by reasonable notice."[25] Whether one analyzes this approach as an enlarged concept of a doctrine of frustration or a new formulation of the rule of construction does not really matter; the fact remains that Lord Denning is in effect making a contract for the parties; that is, he is constructing a contract, notwithstanding that he says "the courts will construe the contract" and he is introducing new rules of construction without direct judicial precedent. In passing it could be mentioned that Lord Denning attempted a similar "construction" of a contract in *Gibson v. Manchester City Council*, but was reversed on appeal to the House of Lords.[26] Nevertheless, as leave to appeal from the Court of Appeal decision in *South Staffordshire* was refused by the House of Lords Appeal Committee,[27] the decision stands.

Boise Cascade Canada Ltd. v. The Queen,[28] a case decided by the Ontario Court of Appeal, has a strikingly similar factual situation. Again there was an agreement of 1905 to supply a town with power "to such an extent as the town may require" at a fixed price and the contract contained no provision as to its duration or for a right to terminate. Some seventy years later the town's population had increased five times

---

[23] *Id.* at 774, [1978] 1 W.L.R. at 1395.

[24] *Id.* at 775 [1978] 1 W.L.R. at 1395.

[25] *Id.* at 775, [1978] 1 W.L.R. at 1395-96.

[26] [1978] 2 All E.R. 583, [1978] 1 W.L.R. 520 (C.A.), *rev'd* [1979] 1 All E.R. 972, [1979] 1 W.L.R. 294 (H.L.).

[27] *Supra* note 22.

[28] 34 O.R. (2d) 18, 15 Bus. L.R. 1, 126 D.L.R. (3d) 649 (C.A. 1981).

and the rate of consumption one hundred and thirty-three times, and the power company found the rate inadequate. It sought a declaration, *inter alia*, that the contract was terminable on reasonable notice.

Mr. Justice Thorson (with Mr. Justice Brooke concurring) refused to follow the *South Staffordshire* case, when invited by counsel for the appellant to "make new law" in Ontario by adopting the approach favoured by Lord Denning. His Lordship agreed with the statement of the trial judge that the law of Ontario on this point is as stated by Viscount Simon in *British Movietonews Ltd. v. London and District Cinemas Ltd.*:

> The parties to an executory contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate — a wholly abnormal rise or fall in prices, a sudden depreciation of currency, an unexpected obstacle to execution, or the like. Yet this does not in itself affect the bargain they have made.[29]

The other issues sought in the declaration were that the appellant should be paid a reasonable price containing an element of profit and that the town was entitled only to a reasonable share of the output of the generating station.

On the issue of price it was held that the language of the agreement made it abundantly clear that the fixed price was a maximum price which was not to be exceeded in any event. The third issue concerning the share was decided by reference to paragraph 13 of the agreement providing for the resolution of certain types of disputes by arbitration. Mme. Justice Wilson, who dissented in part, stated in the course of her judgment:

> Business agreements must be construed in a business-like way. And if that result cannot be reached through the process of interpretation of the agreement. . . then a provision to that effect should be implied into it in order to give it the "business efficacy" the parties must have intended it to have.[30]

This is a far more flexible approach to the construction of documents than that adopted by the majority and it echoes some of the views expressed by Lord Denning in the *South Staffordshire* case.

On appeal to the Supreme Court of Canada, Mr. Justice Estey, speaking for the Court, affirmed the decision of the Court of Appeal regarding the price.[31] His Lordship quoted the *dictum* of Viscount Simon[32] and stated that the parties have specified the extent of their obligation in the terms of the agreement, and it cannot be said that they did not agree to be bound in the circumstances that have arisen. He found it unnecessary, therefore, to consider the *controversial*[33] decision of the English Court of Appeal in the *South Staffordshire* case.[34]

As the Supreme Court of Canada followed the principles of construction stated in *British Movietonews Ltd. v. London and District*

---

[29] [1952] A.C. 166, at 185, [1951] 2 All E.R. 617, at 625 (H.L. 1951).

[30] *Supra* note 28, at 41, 15 Bus. L.R. at 32-33, 126 D.L.R. (3d) at 673.

[31] Town of Fort Frances v. Boise Cascade Canada Ltd., 46 N.R. 108, 143 D.L.R. (3d) 193 (S.C.C. 1983), *rev'g* Boise Cascade Canada Ltd. v. The Queen, *supra* note 28.

[32] *Supra* note 29.

[33] Emphasis added.

[34] *Supra* note 31, at 128, 143 D.L.R. (3d) at 209.

Cinemas Ltd.,[35] it follows that in contracts of indefinite duration the Canadian courts will not be able to provide relief where such contracts become inequitable due to the passage of time. Although the *South Staffordshire* case was not formally overruled, the Supreme Court, by refusing to consider it, clearly indicated its disfavour of Lord Denning's approach to contracts in perpetuity.

C. *Formation of Contracts*

It is commonplace that the basis of a contract is an agreement which usually results from the acceptance of an offer. There are, however, situations where there is clearly an agreement, but it cannot be readily analyzed into an offer and acceptance. There are other situations where it is not clear whether an agreement resulted from a set of negotiations or perhaps from an exchange of documents between the parties, and, if an agreement was reached, it is not always clear what its terms are. One example is the familiar "battle of forms". There are other instances when it is difficult to determine the mode of the formation of the agreement, as for example in the cases of vending machines selling goods, parking tickets and contracts of insurance, and in cases dealing with tenders.

These matters were considered in three cases, by the English Court of Appeal, the House of Lords and the Supreme Court of Canada respectively.

Butler Machine Tool Co. v. Ex-Cell-O Corp. (England)[36] was a decision of the English Court of Appeal dealing with the "battle of forms". The "battle of forms" is often the result of the modern commercial practice of sending printed quotation forms and placing orders with conditions, frequently printed in small print on the reverse side. The businessmen do not read these conditions and if there is an agreement as to essential terms, such as quantity, price, delivery, usually contained on the front page of quotations and orders, they consider they have a contract. The question then arises which of the often contradictory conditions govern the contract? In this case, the sellers, Butler Machine Tool Company, started by making an offer. The offer, in the form of a quotation, contained in small print a clause that orders are accepted only subject to conditions stated in the quotation. One of the conditions was a price variation clause. The buyers, Ex-Cell-O, gave an order which stated, "Please supply on terms and conditions as below and overleaf."[37] The sellers acknowledged the receipt of the official order and no doubt the contract was then concluded. But which set of conditions governed the contract?

Lord Denning cited the trial judge who had held that the conditions, including the price variation clause, set in the seller's quotations, formed

[35] *Supra* note 29.

[36] [1979] 1 All E.R. 965, [1979] 1 W.L.R. 401 (C.A. 1977).

[37] *Id.* at 967, [1979] 1 W.L.R. at 403.

part of the contract. He further said that:

> The sellers did all that was necessary and reasonable to bring the price variation clause to the notice of the buyers. He [the trial judge] thought that the buyers would not "browse over the conditions" of the sellers and then, by printed words in their (the buyers) document, trap the sellers into a fixed price contract.[38]

Lord Denning thought that the judge was influenced by the passages in Anson's *Law of Contract*[39] and in Treitel's *The Law of Contract*[40] which state in effect that in determining which conditions are incorporated in the contract one has to look at all the documents in order to determine which terms the parties would reasonably conclude to form part of the contract.

Lord Denning rejected the judge's approach and applied the orthodox concept of offer, counter-offer and acceptance, as formulated some 130 years ago in *Hyde v. Wrench.*[41] The quotation by the sellers was "killed" by the order of the buyers, which constituted a counter-offer which was accepted by the acknowledgment of the sellers. Lord Denning stated that "as a matter of construction. . . the acknowledgment. . . is the decisive document. It makes it clear that the contract was on the buyers' terms and not on the sellers' terms. . . ."[42] Lords Lawton and Bridge agreed with Lord Denning and leave to appeal to the House of Lords was refused. It would appear that in England at least, the "battle of forms" cases are to be decided according to the well established doctrines of offer, counter-offer and acceptance, and it will be the last accepted form which will govern the contract.

Gibson v. Manchester City Council,[43] a judgment of the House of Lords reversing the decision of the Court of Appeal, dealt with the problem of whether there was a contract in a situation where it was difficult or impossible to analyze the transaction in terms of offer and acceptance. The Manchester Corporation had a policy of selling council houses to its tenants. Mr. Gibson, a tenant of a council house, wanted to buy it. Correspondence was exchanged between the parties, but before a contract was formally prepared, there was a political change in the council and the policy of selling council houses was discontinued. The only issue on appeal was whether the correspondence between the parties resulted in a legally enforceable contract. The county court judge and the Court of Appeal held that it did. In the Court of Appeal, Lord Denning (Ormrod L.J. concurring) adopted a novel approach to the construction of documents. As the conventional approach of the offer and acceptance presented difficulty, Lord Denning said that in such cases:

> You should look at the correspondence as a whole and at the conduct of the parties and see therefrom whether the parties have come to an agreement

---

[38] *Id.* at 966–67, [1979] 1 W.L.R. at 402.
[39] ANSON'S LAW OF CONTRACT 39–40 (25th ed. A. Guest 1979).
[40] G. TREITEL, THE LAW OF CONTRACT 16–18 (6th ed. 1983).
[41] 3 Beav. 334, 49 E.R. 132 (Rolls Ct. 1840).
[42] *Supra* note 36, at 969, [1979] 1 W.L.R. at 405.
[43] [1979] 1 All E.R. 972, [1979] 1 W.L.R. 294 (H.L.).

> on everything that was material. If by their correspondence and their conduct you can see an agreement on all material terms, which was intended thenceforward to be binding, then there is a binding contract in law even though all the formalities have not been gone through.[44]

Lord Denning also held that additional conditions not mentioned in the correspondence or known to Mr. Gibson should be imported into the agreement, such as prohibitions against use except as a dwelling house and against sale within five years. These came from the standard form agreement for sale of a council house utilized in previous sales.

In the House of Lords, Lord Diplock rejected Lord Denning's approach. In his view the question could be decided "by applying to the particular documents relied on. . . as constituting the contract, well settled, indeed elementary, principles of English law."[45] Lord Diplock recognized that there are certain contracts which do not fit easily into the normal analysis in terms of offer and acceptance, but a contract alleged to have been made by exchange of correspondence, in which successive communications are in reply to one another, is not one of these. His Lordship saw no reason for departing from the conventional approach of examining the documents to determine whether on their true construction there was an offer to sell the house by the Council and the acceptance of that offer by Mr. Gibson.[46] The other Law Lords concurred, with Lord Edmund-Davies commenting that this was "a hard case, and we all know where hard cases can take a judge",[47] an obvious allusion to the adage "hardship case makes a bad law".

In his terse speech, Lord Russel stated that the alleged contract was based on an offer by the council contained in a letter to Mr. Gibson and accepted by him. Thus is was a plain case of a contract constituted by offer and acceptance and His Lordship saw no relevance in the general references to consensus contained in the judgment of the Court of Appeal. His Lordship continued that he could not consider "a letter which says that the possible vendor 'may be prepared to sell the house to you'. . . as an offer to sell capable of acceptance so as to constitute a contract."[48]

The judgment of the House of Lords indicates that there is no room for vague notions of intent or consensus to be implied by the court where the clear language of the documents shows that no definite agreement has been concluded. Furthermore, the court cannot make a contract for the parties by imposing conditions not stated in the documents and not in the mind of at least one of the contracting parties other than those arising by necessary implication.

The Queen v. Ron Engineering & Construction (Eastern) Ltd.[49] is a case where a contractor submitted a tender containing a mistake. The

---

[44] *Id.* at 979, [1979] 1 W.L.R. at 302.
[45] *Id.* at 973, [1979] 1 W.L.R. at 295-96.
[46] *Id.* at 974, [1979] 1 W.L.R. at 297.
[47] *Id.* at 976, [1979] 1 W.L.R. at 299.
[48] *Id.* at 980, [1979] 1 W.L.R. at 304.
[49] [1981] 1 S.C.R. 111, 119 D.L.R. (3d) 267.

decision has been adversely commented upon[50] for its analysis of tenders and the treatment of mistake. In our discussion we are concerned only with the analysis of the legal nature of tenders.

Pursuant to a call for tenders, a contractor submitted a tender together with the required tender deposit of $150,000. According to the rules applicable, this deposit would be forfeited if the tender were withdrawn, or if, after acceptance, the bidder did not execute the agreement to perform. After the opening of the tenders, but before any acceptance, the contractor discovered that, by mistake, an amount in excess of $700,000 was not included in the sum tendered. The contractor immediately notified the Water Resources Commission (who had called the tenders). The Commission nevertheless submitted to the contractor an agreement for the performance of the work tendered for the understated amount which the Commission knew to be the result of a mistake. The contractor refused to execute the agreement and the Commission retained the deposit, relying on the terms contained in the call for tenders, providing for the forfeiture of the deposit where a tender is withdrawn or an agreement not executed.

In the action for the recovery of the tender deposit, the Ontario Court of Appeal, reversing the trial judge, held "when that mistake is proven by the production of reasonable evidence, the person to whom the tender is made is not in a position to accept the tender or to seek to forfeit the bid deposit."[51] The Court of Appeal followed its own judgment in *Belle River Community Arena Inc. v. W.J.C. Kaufmann Co.*,[52] holding that an offeree cannot accept an offer which he knows has been made by mistake which affects a fundamental term of the contract. This reasoning is based on a line of cases commencing with *Smith v. Hughes* (the oats case).[53]

The Supreme Court of Canada reversed the Court of Appeal.[54] According to Mr. Justice Estey, a call for tenders is an offer and the submission of a tender is the acceptance of that offer. Upon the submission of the tender, a unilateral contract comes into existence. Mr. Justice Estey used the example, "I will pay you a dollar if you cut my lawn."[55] His Lordship noted that there is no obligation on anybody to cut the lawn and the promise to pay one dollar becomes binding only upon the performance of the invited act, that is, the cutting of the lawn. By analogy, the call for tenders creates no obligation on anybody and the lodging of a tender is the performance. Thus a unilateral contract arises auto-

---

[50] Swan, *Contracts-Mistakes-Irrevocable Tenders in the Construction Industry — The Queen v. Ron Engineering & Construction (Eastern) Ltd.*, 15 U.B.C.L. REV. 447 (1981); Blom, *Mistaken Bids: The Queen in Right of Ontario v. Ron Engineering and Construction Eastern Ltd.*, 6 CAN. BUS. L.J. 80 (1981).

[51] Ron Eng'r. & Constr. (Eastern) Ltd. v. The Queen, 24 O.R. (2d) 332, at 334, 98 D.L.R. (3d) 548, at 551 (C.A. 1979).

[52] 20 O.R. (2d) 447, 87 D.L.R. (3d) 761 (C.A. 1978).

[53] L.R. 6 Q.B. 597, [1861–73] All E.R. Rep. 632 (1871).

[54] *Supra* note 49.

[55] *Id.* at 122, 119 D.L.R. (3d) at 274.

matically on the filing of a tender in response to the call and such contract is governed by the terms contained in the call for tenders. The terms may contain provisions for the irrevocability of the tender, forfeiture of deposit, *etc.* This contract, which regulates solely the formalities of the submission of a tender, is referred to by Estey J. as contract A. Acceptance of a tender results in another contract, dealing with the performance of the work tendered for, in this instance a construction contract. This contract is designated as contract B.

This is certainly a novel approach to the formation of contracts by tender. The generally accepted view is that a call for tenders is a mere invitation to treat, to do business. A tender is an offer, the terms of which become a contract upon acceptance by the caller.[56] Being an offer, such tender is revocable at any time before acceptance, unless it is under seal or consideration has been given.

In respect of irrevocability, the judgment contains the following intriguing statement, "The significance of the bid in law is that it at once becomes irrevocable if filed in conformity with the terms and conditions under which the call for tenders was made and if such terms so provide."[57] As mentioned above, Estey J.'s theory is that a tender constitutes a unilateral contract regulated by the terms of the call. If such terms provide for the irrevocability of the tender, then it is irrevocable. This seems at first glance quite logical, accepting the theory of unilateral contract. The problem, however, is that it goes contrary to the traditional concept of irrevocability of offers not in the form of an option.[58] Does it mean that every bid is irrevocable if the call so provides? Does this concept extend to any offer where either the offer states that it is irrevocable or the invitation asks for an irrevocable offer? If that is so, then this decision of the Supreme Court has abolished some long established principles of common law.

Mr. Justice Estey did not cite any cases or texts in support of his analysis of tenders as unilateral contracts. There are several problems arising from this new theory. Firstly, assuming that this new theory applies to tenders only, how does one distinguish between a tender and an offer? Is an offer transformed into a tender when it is so called? For example, A writes to several suppliers asking for tenders (or offers) to supply goods. Are their replies offers or tenders, depending on what they are called? What about the contracts? Do the replies, when accepted, become contracts for supply of goods, or are the replies only formal contracts of type "A" and is it necessary to execute an additional contract

[56] *Cf.* 9 HALSBURY, LAWS (4th) para. 230 and cases quoted therein; ANSON'S LAW OF CONTRACT, *supra* note 39, at 27, 51; CHESHIRE AND FIFOOT'S LAW OF CONTRACT 39–40 (10th ed. M. Furmstrom 1976); FRIDMAN, THE LAW OF CONTRACT 55 (1976); and Canadian case law: Belle River Community Arena v. W.J.C. Kaufman Co., 20 O.R. (2d) 447, 87 D.L.R. (3d) 761 (C.A. 1978); Imperial Glass Ltd. v. Consolidated Supplies Ltd., 22 D.L.R. (2d) 759 (B.C.C.A. 1960).

[57] *Supra* note 49, at 122, 119 D.L.R. (3d) at 274–75.

[58] *Cf.* Goldsborough Mort. & Co. v. Quinn, 10 N.S.W. St. R. 170, 10 C.L.R. 674 (Full Ct. 1910); Dickinson v. Dodds, 2 Ch. 463, 24 W.R. 595 (C.A. 1876).

of type "B"? There are also problems with promise and consideration. The submission of a tender can well be perceived as the performance of an act, but in response to what promise? In the example given, the promise is the payment of one dollar, but what is the promise here? One possible argument is that the caller promises to receive and consider the tenders, but that appears to be a rather artificial construction of a promise. Another aspect is the consideration contained in the promise. A man cuts a lawn for the promise of one dollar; a contractor submits a tender — for what? The caller for tenders may or may not accept the tender; there is no obligation on his part crystallizing upon the submission of the tender. Again, one could argue that the contractor has the benefit of his tender being considered or that the caller has a duty or detriment of examining the tenders, but is this real consideration?

Another conceptual problem is that requests for quotations, catalogues, price lists, display of goods, *etc.* are traditionally considered as invitations to do business and not as binding offers capable of acceptance. This is a well established principle of common law.

The disposition of the case should be mentioned in passing. It was held that there was no mistake at the time when the unilateral contract "A" came into existence. The contractor intended to submit the tender in that form and substance. The mistaken estimate might have effect on the validity of contract "B", the construction contract, but that contract never came into existence. As the contractor refused to execute the construction contract "B", he forfeited the deposit under the terms of contract "A". It follows from the judgment that when a contractor makes a mistake in his tender under similar conditions, as to irrevocability and forfeiture of deposit, he has no remedy, except possibly to execute contract "B" and then bring an action to have it declared void because of the mistake. While the Supreme Court reversed the decision of the Court of Appeal, the *Belle River* case, which the Court of Appeal followed, was not expressly overruled, although it was probably overruled by implication.

The Ontario Court of Appeal recently considered the problems of tenders and collateral contracts in *Kawneer Co. Canada Ltd. v. Bank of Canada*.[59] The plaintiff tendered for the erection of an exterior glass curtain wall, part of the new Bank of Canada building. The Bank invited tenders based upon performance specification leaving it to the bidders to provide proposals which would satisfy performance criteria. The danger inherent in this type of invitation to tender is a practice called "low balling". A builder could submit an attractive low price but fail to supply the detailed design and engineering information required to meet the performance criteria. The plaintiff was aware of that and wanted to protect himself. He sought assurances that the main factors in the evaluations would be the completeness and competence of the bids and not the price. He sought such assurances at a meeting with the Bank's representative prior to tendering and he was satisfied that he received

[59] 40 O.R. (2d) 275 (C.A. 1982).

such oral assurances. He bid in reliance on these assurances but was not successful and the contract was awarded to the lowest bidder.

Kawneer brought an action for damages claiming that terms of the collateral contract, established by the oral assurances, were breached by the defendant and that the defendant also breached the terms of the invitations to tender. The Court of Appeal, affirming the decision of the trial judge, held that there was no evidence of the collateral contract and that the terms of the invitation to tender were not breached by the defendant. This decision depended largely on the facts of the case.

More interesting, from the legal point of view, is the treatment of the *Ron Engineering* case[60] by the Court of Appeal. First, the Court was not quite consistent in its interpretation of this case. It stated in the first reference to the case that the Supreme Court of Canada decision recognized that contractual obligations distinct from the construction contract may arise from the tendering process.[61] Later reference states, "The Supreme Court held that these provisions constituted a 'unilateral contract' binding the tenderer. . . . The contract came into effect when the tender was submitted."[62] This later reference correctly reflects the Supreme Court decision, which does not recognize that contractual obligations distinct from the construction contract may arise. It clearly states that upon the submission of a tender in response to an invitation to bid a unilateral contract comes into existence. Next, the Court of Appeal stated that it is trite law that an invitation to tender is merely an offer to negotiate and that the submission of a tender constitutes an offer which, if accepted, becomes a binding contract.[63] This is the orthodox understanding of invitations and tenders, but not the theory of Mr. Justice Estey. The Court of Appeal is clearly uneasy about this novel theory but was able to resolve its dilemma in this case by finding that as the terms of the invitation to tender had been complied with, it was unnecessary to consider whether the decision in the *Ron Engineering* case applied.[64]

II. Promissory Estoppel

A. *Sword/Shield Distinction*

Two aspects of the doctrine of promissory estoppel have recently been considered by Canadian courts. These are whether promissory estoppel can be used as a cause of action and whether detrimental reliance by the promisee is essential.

Until recently it was generally accepted that promissory estoppel alone cannot give rise to a cause of action so as to do away with the necessity of consideration, but can only be used as a defence to prevent a party from insisting on his strict legal rights when it would be unjust to

[60] *Supra* note 49.
[61] *Supra* note 59, at 283.
[62] *Id.* at 284.
[63] *Id.* at 283.
[64] *Id.* at 286.

allow him to do so. This principle is sometimes summed up in the maxim that *estoppel can never be used as a sword but only as a shield.* This principle was mentioned in the *High Trees* cases,[65] elaborated on by Lord Denning in *Combe v. Combe*[66] and affirmed in Canada by the Supreme Court in *Canadian Superior Oil Ltd. v. Paddon-Hughes Development Ltd.*[67] The principle was also affirmed by the Ontario Court of Appeal in *Gilbert Steel Ltd. v. University Construction Ltd.*[68] and has been commonly stated in the literature.[69]

In some of the recent decisions of the Ontario courts there appears a tendency to move away from this restrictive application of the doctrine. In *Re Tudale Explorations Ltd. and Bruce*,[70] Mr. Justice Grange stated that the sword/shield maxim has been heavily criticized and that he must confess to difficulty in seeing the logic of this distinction.[71] In that case, however, the promise was set up as a shield and not as a sword. Mr. Justice Grange mentioned the sword/shield distinction again in *Petridis v. Shabinsky*.[72] His Lordship's *dicta* there seemed to indicate that the doctrine of promissory estoppel can be used as a sword to establish a claim.[73] In *M.L. Baxter Equipment Ltd. v. Geac Canada Ltd.*,[74] Mr. Justice Rutherford said that great doubt has recently been cast on the sword/shield distinction and that *Conwest Exploration Co. v. Letain*[75] and *Re Tudale Exploration Ltd. and Bruce*[76] leave little hope for the continuation of this distinction.[77] Finally, in *Edwards v. Harris-Intertype (Canada) Ltd.*, Mr. Justice Osborne explained the position as follows:

> It is apparent the weight of authority prior to the *Tudale* decision was that promissory estoppel could be used solely as a defence, and could not be asserted as a cause of action. None of the decisions since *Gilbert Steel* unequivocally state that estoppel may constitute a cause of action, but many move in that direction.[78]

Although each of the cases discussed was decided on different grounds and the statements referred to are *obiter dicta*, they are nonetheless portent indicators of possible future developments of the doctrine of promissory estoppel.

---

[65] Central London Property Trust Ltd. v. High Trees House Ltd., [1947] K.B. 130, [1946] 1 All E.R. 256 (K.B. 1946).

[66] [1951] 2 K.B. 215, [1951] 1 All E.R. 767 (C.A.).

[67] [1970] S.C.R. 932, 12 D.L.R. (3d) 247.

[68] 12 O.R. (2d) 19, at 23-24, 67 D.L.R. (3d) 606, at 610-11 (C.A. 1970).

[69] *Cf.* ANSON'S LAW OF CONTRACT, *supra* note 39, at 116; FRIDMAN, THE LAW OF CONTRACT, *supra* note 56, at 194-95.

[70] 20 O.R. (2d) 593, 88 D.L.R. (3d) 584 (Div. Ct. 1978).

[71] *Id.* at 597, 88 D.L.R. (3d) at 588.

[72] 35 O.R. (2d) 215, 132 D.L.R. (3d) 430 (H.C. 1982).

[73] *Id.* at 221, 132 D.L.R. (3d) at 435-36.

[74] 36 O.R. (2d) 150, 133 D.L.R. (3d) 372 (H.C. 1982).

[75] [1964] S.C.R. 20, 41 D.L.R. (2d) 198.

[76] *Supra* note 70.

[77] *Supra* note 74, at 158, 133 D.L.R. (3d) at 381.

[78] 40 O.R. (2d) 558, at 570 (H.C. 1983).

B. *Reliance*

There is another aspect of the doctrine of promissory estoppel in respect of which Canadian courts hold firm; that is, that the promisee must have relied upon the promise to his detriment. The origin and formulation of this requirement are unclear. In *Hughes v. Metropolitan Railway Co.*[79] this requirement was satisfied since the respondents refrained from carrying on repairs in reliance on the promise and thus breached the terms of a lease. Lord Cairns, in his formulation of the principle, referred to "the dealings which have thus taken place between the parties"[80] but not to any detriment to the promisee. There was clearly no detrimental reliance by the promisee in the *High Trees* case[81] and the requirement of detriment was not even mentioned. Lord Denning himself later admitted that there was no detriment[82] and, in *Allen (W.J.) & Co. v. El Nasr Co.*,[83] rejected the requirement that there must be detriment, stating that all that is required is that one should have acted on the belief induced by the other party.[84]

The Canadian courts, on the other hand, fairly consistently refer in their formulation of the requirements of promissory estoppel to detriment. Thus reference to detriment is found in *Gilbert Steel Ltd. v. University Construction Ltd.*,[85] *Re Tudale Explorations Ltd. and Bruce*,[86] *M.L. Baxter Equipment v. Geac Canada*,[87] to mention but a few recent cases. The Supreme Court of Canada affirmed the requirement of detriment in the *Canadian Superior Oil* case[88] and Mr. Justice Estey in the recent case of *Fort Frances v. Boise Cascade*[89] stated that it seems clear that promissory estoppel operates where a promise or representation has been relied upon to the detriment of the person to whom it was directed.[90]

It is to be noted that none of the above cases mention Lord Denning's expositions in the *El Nasr* case[91] or the doubts about the requirement of detriment expressed in most leading texts.[92]

---

[79] [1876-77] A.C. 439, [1874-80] All E.R. 187 (H.L. 1877).

[80] *Id.* at 448, [1874-80] All E.R. at 191.

[81] *Supra* note 65.

[82] Denning, *Recent Developments in the Doctrine of Construction*, 15 MODERN L. REV. 1, at 6-8 (1982).

[83] [1972] 2 Q.B. 189, [1972] 2 All E.R. 127 (C.A.).

[84] *Id.* at 213, [1972] 2 All E.R. at 140.

[85] *Supra* note 68.

[86] *Supra* note 70.

[87] *Supra* note 74, at 152, 133 D.L.R. (3d) at 382.

[88] *Supra* note 67, at 939, 12 D.L.R. (3d) at 253.

[89] 46 N.R. 108 (S.C.C. 1983).

[90] *Id.* at 136-37.

[91] *Supra* note 83.

[92] *See* ANSON'S LAW OF CONTRACT, *supra* note 40; G.H. TREITEL, THE LAW OF CONTRACT, 85, 94 (5th ed. 1979).

III. NON EST FACTUM

Non est factum, which is an abbreviation of a legal maxim *Scriptum predictum non est factum suum*, is a plea which permits one who has signed a written document, which is essentially different from that which he intended to sign, to plead that "it is not his deed" in contemplation of the law.[93]

In its modern form the plea was stated by Mr. Justice Byles in *Foster v. Mackinnon*:

> It seems plain, on principle and on authority that, if a blind man or a man who cannot read, or who for some reason (not implying negligence) forbears to read, has a written contract falsely read over to him, the reader misreading to such a degree that the written contract is of a nature altogether different from the contract pretended to be read from the paper which the blind or illiterate man afterwards signs; then, at least if there be no negligence, the signature so obtained is of no force. And it is invalid not merely on the ground of fraud where fraud exists, but on the ground that the mind of the signer did not accompany the signature; in other words, that he never intended to sign, and therefore in contemplation of law never did sign, the contract to which his name is appended.[94]

With the passage of time this formulation became encrusted with some interpretations which altered the original concept. Of these, two are most prominent, the negligence of the signor and the degree of difference required.

A. *Negligence*

It is clear from the law, as laid down in *Foster v. Mackinnon*, that a person who signed a document differing fundamentally from that which he believed it to be would be disentitled from successfully pleading *non est factum* if his signing was due to his own negligence. The word "negligence" in this connection had no special or technical meaning. It meant carelessness, and in each case it was a question of fact for the jury to decide whether the person relying on the plea had been negligent.

This view of negligence became distorted in the case of *Carlisle and Cumberland Banking Co. v. Bragg*.[95] In this case the defendant was induced by fraud to sign a guarantee believing that it was a mere proposal of insurance. Although the jury found that he was negligent, the trial judge considered that the finding of negligence was immaterial and the Court of Appeal upheld the view. As a result of this decision the negligence of the signor is irrelevant except as regards bills of exchange, where the original formulation in *Foster v. Mackinnon*[96] applies. *Carlisle v. Bragg*[97] was adopted by the majority of the Supreme Court of Canada,

---

[93] ANSON'S LAW OF CONTRACT, *id.* at 313.
[94] L.R. 4 C.P. 704, at 711, 38 L.J.C.P. 310, at 315 (1869).
[95] [1911] 1 K.B. 489, 80 L.J.K.B. 472 (1910).
[96] *Supra* note 94.
[97] *Supra* note 95.

Mr. Justice Cartwright dissenting, in *Prudential Trust Co. v. Cugnet.*[98]

B. *Degree of Difference*

Foster v. Mackinnon speaks of a written contract of a nature altogether different from the contract pretended.[99] Over a period of time a distinction between nature and contents of the document crept in,[100] making the plea successful only where there was a mistake as to the essential nature of the document as distinct from the mistake as to the contents.

The doctrine of *non est factum* was thoroughly examined and restated by the House of Lords in *Saunders v. Anglia Building Society.*[101] The decision may be summarized as follows:

1. The law was put back to the position in which it was after *Foster v. Mackinnon.* In particular the formulation of Byles J. in that case was approved as containing the essential features of the doctrine and not requiring any radical transformation.
2. *Carlisle v. Bragg* was overruled and held to be wrong in reasoning and decision. The word "negligence" in this context does not have the same meaning as in tort; it means carelessness and in each case it is a question of fact whether a person pleading *non est factum* has been negligent. When negligence (that is, carelessness) is found, then *non est factum* is not available.
3. The distinction between nature and contents was disapproved and the House of Lords laid down a new test of the difference. It was suggested that the difference between the document signed and the document as misrepresented must be "radical", "fundamental", "serious", "very substantial", or "total".
4. It was explained that it is inaccurate and misleading to say that the plea of *non est factum* operates by way of estoppel. It is not a true estoppel, but an illustration of the principle that no man can take advantage of his own wrong.

Several Canadian courts have dealt with the plea of *non est factum* since the House of Lords decision. In *Commercial Credit Corporation Ltd. v. Carroll Brothers Ltd.*,[102] the question whether *Saunders v. Anglia Building Society*[103] applies in Canada was not decided, but in a number of subsequent cases the principles laid down by the House of Lords were followed.[104]

---

[98] [1956] S.C.R. 914, 5 D.L.R. (2d) 1.

[99] *Supra* note 79.

[100] *Cf.* Howatson v. Webb, [1907] 1 Ch. 537, 77 L.J.ChD. 32, *aff'd* [1908] 1 Ch. 1; Markham Finance Ltd. v. Howard, [1963] 1 Q.B. 904.

[101] [1971] A.C. 1004, [1970] 3 All E.R. 961 (H.L. 1970), *aff'g* Gallie v. Lee, [1969] 1 All E.R. 1062 (C.A.).

[102] 20 D.L.R. (3d) 504 (Man. C.A. 1971).

[103] *Supra* note 101.

[104] *Cf.* Canadian Imperial Bank of Commerce v. Kanadian Kiddee Photo Ltd., [1979] 3 W.W.R. 256 (B.C.C.A.); Royal Bank of Canada v. Poisson, 26 O.R. (2d) 717,

In *Marvco Color Research Ltd. v. Harris*,[105] Mr. Justice Grange of the Ontario Supreme Court found that the defendants pleading *non est factum* were careless in not reading the document before signing. Nevertheless, His Lordship held that the plea was available as he was bound to follow the Supreme Court of Canada decision in *Prudential Trust v. Cugnet*.[106] His Lordship appreciated that the House of Lords in *Saunders v. Anglia Building Society*[107] overruled *Carlisle and Cumberland v. Bragg*[108] and he was attracted by the dissenting judgment of Cartwright J. in *Prudential Trust v. Cugnet*.[109] He also quoted several Canadian cases following *Saunders*. Still, he felt bound by *Prudential Trust v. Cugnet*. The Ontario Court of Appeal dismissed an appeal, affirming Grange J.'s reasons. The Court of Appeal also expressed concern about the principle in issue, but like Grange J. it felt bound to follow *Prudential Trust v. Cugnet*.[110]

A further appeal to the Supreme Court of Canada provided an opportunity to review the law. Mr. Justice Estey, speaking for the Court, allowed the appeal. His Lordship reviewed the development of *non est factum* in England and Canada; followed *Saunders* on the issue of negligence; disagreed with the reasoning in *Carlisle and Cumberland v. Bragg*; and overruled *Prudential Trust v. Cugnet*. His Lordship referred in particular to the dissenting judgment of Cartwright J. in that case, which in his view correctly enunciated the principles of the law of *non est factum*. Mr. Justice Cartwright had refused to follow *Carlisle and Cumberland v. Bragg* and concluded that any person who fails to exercise reasonable care in signing a document is precluded from relying on the plea of *non est factum*.[111]

Mr. Justice Estey found it unnecessary to concern himself with other aspects of the judgment in *Saunders*, but noted in passing the new, more flexible test of the degree of difference formulated by the Law Lords and the rejection of the distinction between nature and contents. He quoted Lord Pearson's phrases "fundamentally different" or "radically different" or "totally different".[112]

Although the Supreme Court of Canada dealt explicitly with only one aspect of the *Saunders* case, that being the principles of negligence, it appears from the tenor of the judgment that the Supreme Court is prepared to follow *Saunders* in other aspects as well.

The attitude of the Canadian courts to the House of Lords' judgment in *Saunders*, whereby some courts follow the case whilst others consider

103 D.L.R. (3d) 735 (Ont. H.C. 1977); Dwinell v. Custom Motors Ltd., 12 N.S.R. (2d) 524, 61 D.L.R. (3d) 342 (N.S.C.A. 1975); Bank of Nova Scotia v. Battiste, 22 Nfld. & P.E.I.R. 192 (Nfld. S.C. 1980).

[105] 27 O.R. (2d) 686, 107 D.L.R. (3d) 632 (Ont. H.C. 1980).

[106] *Supra* note 98.

[107] *Supra* note 101.

[108] *Supra* note 95.

[109] *Supra* note 98, at 929, 5 D.L.R. (2d) at 5.

[110] 30 O.R. (2d) 162, 115 D.L.R. (3d) 512.

[111] *Supra* note 98.

[112] 45 N.R. 302 (S.C.C. 1982).

themselves bound by a previous contrary decision of the Supreme Court of Canada,[113] poses an intriguing problem: What is the law in this area? The choice seems to lie between an old decision of the Supreme Court of Canada and a recent contrary decision of the House of Lords, which is well reasoned and generally accepted as being a proper statement of the law. To put the problem in other words: Can courts other than the Supreme Court of Canada initiate changes in the law?

IV. Contractual Terms

The most significant developments of the law of contracts are in the area of contractual terms. Lord Roskill, for example, referred to the judgment of Lord Diplock in *Hongkong Fir Shipping Co. v. Kawaski Kisen Kaisha Ltd.*[114] as "a landmark in the development of one part of our law of contract."[115] This area shall be examined under the following headings: terms — their construction and effect, exemption clauses, collateral contracts and negligent misrepresentations. The doctrine of parol evidence will also be discussed.

A. *Terms — Their Construction and Effect*

Prior to the judgment of Lord Diplock in *Hongkong Fir*, contractual terms were traditionally treated as either conditions or warranties. This dichotomy became firmly established by the Sale of Goods Act 1893[116] and the judgment of Bowen L.J. in *Bentsen v. Taylor Sons & Co.*,[117] and since that time these two words have been used as terms of art. Previously there had been considerable confusion.

Through a well reasoned historical analysis, Lord Diplock showed in his judgment that the dichotomy is not well founded and that there is a third category, an innominate term.[118] Every synallagmatic contract (that is, a contract imposing reciprocal obligations) presents a problem as to the circumstances in which a party will be relieved from his obligation to perform. Lord Diplock stated that this could be determined in three ways: the contract itself may define some of these events, in other words, the parties may stipulate that certain terms are conditions; or Parliament may define the conditions by statute (for example, implied conditions under the Sale of Goods Act); or the court will have to decide which term will have that effect. The court will apply this test: does the event deprive the party not at fault of substantially the whole benefit of

---

[113] *See* the cases cited at note 104 *supra*.

[114] [1962] 2 Q.B. 26, at 65, [1962] 1 All E.R. 474, at 485 (C.A. 1961).

[115] Bunge Corp. v. Tradax SA, [1981] 2 All E.R. 513, at 550, [1981] 1 W.L.R. 711, at 725 (H.L.).

[116] 56 & 57 Vict., c. 71.

[117] [1893] 2 Q.B. 274, at 280, 63 L.J.Q.B. 15, at 17 (C.A.).

[118] *Supra* note 114.

the contract? Lord Diplock stressed that it was really the event resulting from the breach, or to put it in other words, the seriousness of the consequences of the breach and not the breach itself, which relieved the party from further performance. He then continued that there are many simple contractual undertakings where it may be predicated that every breach of such undertaking will result in the loss of substantially the whole benefit of the contract, that there are other undertakings where the opposite applies, and finally that there is a third category where one cannot so predicate. For this third category, the term innominate or indeterminate was later used. For terms of this class, the consequences of a breach cannot be predicated and, unless provided for expressly in the contract, the legal consequences will be determined by the events resulting from the breach.

This tripartite division of contractual terms was followed in subsequent cases, most notably in *Cehave N.V. v. Bremer*[119] where the Court of Appeal applied and further analyzed the *Hongkong Fir* case. However, Lord Diplock's analysis gradually came to be interpreted in a way not probably intended; specifically, unless a term was expressly designated as a condition, it was an innominate term and there was no right to repudiate the contract unless there was a loss of substantially the whole benefit of the contract. That this interpretation was not intended by Lord Diplock is obvious from his judgment in *Photo Production Ltd. v. Securicor Transport Ltd.*,[120] where he distinguished between fundamental breach and a breach of a condition. The first term, fundamental breach, is to be confined to an event whereby the other party is deprived of substantially the whole benefit of the contract. The term "condition" is to be used where the parties have agreed, either expressly or by implication of law, that any particular failure to perform, irrespective of the gravity of the consequences, shall entitle the party not at fault to put an end to his performance.

The case of *Bunge Corporation v. Tradax SA*[121] gave the House of Lords an opportunity to re-examine Lord Diplock's analysis. The facts are simple: Bunge entered into a contract with Tradax for the purchase of 15,000 tons of soya beans to be delivered in three consignments. The buyers were required to provide a ship at a nominated port and to give at least fifteen consecutive days notice of the readiness of the vessel. Bunge gave only fourteen days notice on the second consignment and Tradax repudiated the contract. The contract was silent as to the legal nature of this clause. Counsel for Bunge, relying on Lord Diplock's judgment in the *Hongkong Fir* case,[122] submitted that as the term was not expressly stated to be a condition, it must be an innominate term and therefore the innocent party can repudiate only where it has been deprived of substantially the whole benefit of the contract. Counsel

[119] [1976] Q.B. 44, [1975] 3 All E.R. 739 (C.A. 1975).
[120] [1980] A.C. 827, at 848–50, [1980] 1 All E.R. 556, at 566–67 (H.L.).
[121] *Supra* note 115.
[122] *Supra* note 114.

further relied on an ensuing passage from the same judgment, which stated that "legal consequences of a breach of such an undertaking, *unless provided for expressly in the contract*, depend on the nature of the event to which the breach gives rise."[123] Counsel argued that there was no express provision in the contract, the event resulting from the breach did not deprive the sellers of substantially the whole benefit of the contract and hence there was no right to repudiate.

The House of Lords unanimously rejected this argument. Lord Roskill found nothing in the judgment of Diplock L.J. in the *Hongkong Fir* case which would suggest any departure from the basic and long-standing rules used for determining whether a particular term in the contract was or was not a condition.[124] In this connection, Roskill L.J. quoted Bowen L.J. in *Bentsen v. Taylor* to the effect that the only way of deciding that question is to look at the contract in the light of surrounding circumstances and then infer the intentions of the parties from the instrument itself.[125] Lord Roskill stated that he did "[n]ot believe that [Lord Diplock] ever intended his judgment to afford an easy escape route from the normal consequences of rescission to a contract breaker who had broken what was, on its true construction, clearly a condition of the contract by claiming that he had only broken an innominate term."[126] He then suggested that the passage from the *Hongkong Fir* case regarding an *express* provision in a contract for the breach of an innominate term[127] should be amended by adding "or impliedly" after "expressly".[128] Lord Roskill supported this recommendation by reference to Lord Diplock's judgment in *Photo Production* where Lord Diplock stated that a contractual term is a condition where the parties have so agreed, either expressly or *by implication*.[129] Having thus explained the construction of the term "condition", the House of Lords held that stipulations as to time in mercantile contracts should be treated as conditions because of the need for certainty in such contracts. Further, where performance of an undertaking by one party is a condition precedent to the performance by the other party, such an undertaking should be treated as a condition.[130]

This judgment re-affirmed Lord Diplock's analysis of contractual terms and further clarified it as regards innominate terms. Such terms are to be treated as conditions, thus giving the right to repudiate the contract, where on a true construction of the contract it appears that this was the intention of the parties and is not restricted to situations where the innocent party has been deprived of substantially the whole benefit of the contract.

---

[123] *Id.* at 70, [1962] 1 All E.R. at 487 (emphasis added).
[124] *Supra* note 115, at 549, [1981] 1 W.L.R. at 725.
[125] *Supra* note 117, at 281, 63 L.J.Q.B. at 18.
[126] *Supra* note 115, at 550, [1981] 1 W.L.R. at 725–26.
[127] *Supra* note 114, at 70, [1962] 1 All E.R. at 487.
[128] *Supra* note 115, at 550, [1981] 1 W.L.R. at 726.
[129] *Supra* note 120, at 849, [1980] 1 All E.R. at 566 (emphasis added).
[130] *Supra* note 115, at 553, [1981] 1 W.L.R. at 729.

B. *Exemption Clauses*

The emergence of standard form contracts or contracts of adhesion, as they are sometimes called, encouraged the increasing use of exemption (or exclusionary) clauses. The courts had to react to the frequent use and abuse of these clauses and one of the problems that preoccupied the courts in the second half of this century was whether an exemption clause should be available when a fundamental breach occurred. For example, a person enters into a contract with a security company to protect his property. One of the employees of the company starts a fire which destroys that property. The contract contains a clause exempting the company from virtually any liability. Could the clause be invoked against what is undoubtedly a fundamental breach?[131] After all, the contract was to secure the protection and not the destruction of the property.

Two theories have held sway, the "rule of law" and the "construction" theory. The "rule of law" theory holds that it is a rule of substantive law that a fundamental breach destroys the effectiveness of an exemption clause. The "construction" theory holds that whether an exemption clause exempts a party from liability on the occurrence of a fundamental breach is a question determined on the true construction of the contract. The "rule of law" theory was put forward by Lord Denning in such cases as *Karsales (Harrow) Ltd. v. Wallis*,[132] *Harbutt's Plasticine Ltd. v. Wayne Tank & Pump Co.*[133] and in his Court of Appeal judgment in *Photo Production*.[134] The "construction" theory was very clearly stated by Pearson L.J. in *U.G.S. Finance Ltd. v. National Mortgage Bank of Greece and National Bank of Greece*,[135] and examined at length and adopted by the House of Lords in the *Suisse Atlantique* case.[136] Both theories were followed in a number of Canadian and English decisions.

After the *Suisse Atlantique* judgment in 1966, the courts paid lip service to the "construction" theory, but the "rule of law" theory continued to be followed in some judgments.[137] It was reintroduced by Lord Denning in the *Harbutt's Plasticine* case and in the Court of Appeal decision in *Photo Production*. The "construction" theory was reaffirmed by the unanimous decision of the House of Lords in *Photo Production Ltd. v. Securicor*[138] which overturned the Court of Appeal judgment and overruled the *Harbutt's Plasticine* case.

The House of Lords held that there is no "rule of law" by which exemption clauses are eliminated, regardless of their terms, where there has been a fundamental breach of contract. The question of whether an

[131] *Supra* note 120.

[132] [1956] 2 All E.R. 866, [1956] 1 W.L.R. 936 (C.A.).

[133] [1970] 1 Q.B. 447, [1970] 1 All E.R. 225 (C.A. 1969).

[134] [1978] 3 All E.R. 146, [1978] 1 W.L.R. 856 (C.A.).

[135] [1964] 1 Lloyd's Rep. 446, 107 Sol. J. 552 (C.A. 1963).

[136] Suisse Atlantique Société d'Armement Maritime S.A. v. N.V. Rotterdamsche Kolen Centrale, [1967] 1 A.C. 361, [1966] 2 All E.R. 61 (H.L. 1966).

[137] *See, e.g.*, Mendelssohn v. Normand Ltd., [1969] 2 All E.R. 1215, [1969] 3 W.L.R. 139 (C.A.).

[138] *Supra* note 120.

exemption clause is to be applied is a matter of construction of the contract. It is interesting to note that both Lord Denning in the Court of Appeal and the Law Lords quoted *dicta* from the *Suisse Atlantique* case in support of their diametrically opposed decisions. It certainly does not say much for the lucidity of the lengthy speeches in *Suisse Atlantique*. Lords Wilberforce and Diplock drew a distinction between consumer and commercial contracts but did not come to any conclusions. Lord Diplock stated:

> My Lords, the reports are full of cases in which what would appear to be very strained constructions have been placed on exclusion clauses, mainly in what today would be called consumer contracts and contracts of adhesion. As Lord Wilberforce has pointed out, any need for this kind of judicial distortion of the English language has been banished by Parliament's having made these kinds of contracts subject to the Unfair Contract Terms Act 1977. In commercial contracts negotiated between businessmen capable of looking after their own interests and of deciding how risks inherent in the performance of various kinds of contract can be most economically borne (generally by insurance), it is, in my view, wrong to place a strained construction on words in an exclusion clause which are clear and fairly susceptible of one meaning only even after due allowance has been made for the presumption in favour of the implied primary and secondary obligations.[139]

It is quite likely that this judgment of the House of Lords will be remembered mainly for Lord Diplock's lucid exposition of the effect of the breach of contract. This exposition was in response to Lord Denning's statements in *Harbutt's Plasticine* and *Photo Production* to the effect that upon the occurrence of the fundamental breach, the contract is at an end and the ending disentitles the guilty party from relying on an exclusion clause.[140]

According to Lord Diplock's analysis, every contract contains primary obligations, that is, what the parties promise to do. Breaches of primary obligations give rise to substituted secondary obligations on the part of the defaulting party. Every failure to perform a primary obligation is a breach of contract and the corresponding secondary obligation which arises on the part of the contract breaker, by implication of the common law, is to pay monetary compensation — damages. This secondary obligation to pay damages is called a "general secondary obligation".

Subject to two exceptions, the primary obligations of both parties are not affected by the breach and they have to be performed. The two exceptions are: (i) where the failure by one party to perform a primary obligation deprives the other party of substantially the whole benefit of the contract — for this event the term "fundamental breach" should be retained; and (ii) where the contracting parties have agreed, expressly or by implication of law, that any failure to perform, irrespective of the consequences, shall give rise to the right to put an end to the contract by

---

[139] *Id.* at 851, [1980] 1 All E.R. at 568.

[140] *Harbutt's Plasticine*, *supra* note 133, at 467, [1970] 1 All E.R. at 235; *Photo Production*, *supra* note 134, at 152, [1978] 1 W.L.R. at 863-64.

the innocent party — for this event the term "condition" should be reserved.

Where either the fundamental breach or the breach of a condition occurs, the party not at fault may make an election to put an end to the contract. If that is the case, both parties are relieved from the unperformed primary obligations but there is substituted, by implication of law, for the unperformed primary obligations of the party in default, a monetary compensation payable to the innocent party for a loss resulting from such non-performance. This monetary compensation, payable in addition to the general secondary obligations, is called an "anticipatory secondary obligation". It should be noted that this analysis is, of course, an *obiter dictum.*

The judgment of the House of Lords was applied by the Ontario Court of Appeal and the Supreme Court of Canada in *Beaufort Realities (1964) Inc. v. Chomedy Aluminum Co.*[141] This judgment has been criticized for its adoption of the House of Lords judgment without an adequate statement of the reasons therefor.[142]

The importance of the House of Lords judgment lies in its reassertion of the principle of freedom of contract in commercial transactions and its emphasis on the construction of contracts to give effect to the true intention of the parties. The question remains whether the courts will genuinely adopt the concept of "construction" or will pay it lip service while following in reality the "rule of law". Doubt has been expressed whether the *Photo Production* decision should apply to non-commercial transactions, such as consumer sales. Although the *Photo Production* situation was a commercial one, there is nothing in the judgment to indicate that it should not have universal application.

Following the *Photo Production* case, the House of Lords dealt with two other cases involving exemption clauses, specifically the *Ailsa Craig* case,[143] referred to as the second *Securicor* case, and the *Finney Lock Seeds* case.[144]

In *Ailsa Craig*, the House of Lords considered principles governing the construction of exemption clauses and drew a distinction between exclusionary clauses and limitation clauses. Two ships berthed in the Aberdeen harbour sank due to the negligence of the Securicor company: the patrolman had gone to celebrate New Year's Eve and the ships were left unattended. Securicor admitted negligence but claimed exemption from liability under two clauses in the contract. The first clause, which purported to exclude liability *in toto*, was held ineffective by the lower

[141] [1980] 2 S.C.R. 718, 116 D.L.R. (3d) 193, *aff'g*, *sub nom.* Chomedy Aluminum Co. v. Belcourt Constr. (Ottawa) Ltd., 24 O.R. (2d) 1, 97 D.L.R. (3d) 170 (C.A. 1979).

[142] *See, e.g.*, Ziegel, *The House of Lords Overrules Harbutt's Plasticine*, 30 U. TORONTO L.J. 421 (1981); Ogilvie, *Photo Production v. Securicor Transport Ltd.: An Inconclusive Unscientific (Canadian) Postscript*, 5 CAN. BUS. L.J. 368 (1981); Waddams, *Note*, 15 U.B.C.L. REV. 189 (1981).

[143] Ailsa Craig Fishing Co. v. Malvern Fishing Co., [1983] 1 All E.R. 101, [1983] 1 W.L.R. 964 (H.L. 1981).

[144] George Mitchell (Chesterhall) Ltd. v. Finney Lock Seeds Ltd., [1983] 2 All E.R. 737, [1983] 3 W.L.R. 163 (H.L.).

courts and abandoned by Securicor. The only issue before the House of Lords was the effectiveness of the second clause which purported to limit the liability to a maximum of £1,000 for any one claim and £10,000 for any aggregate of claims.

Lord Wilberforce stated:

> Whether a condition limiting liability is effective or not is a question of construction of that condition in the context of the contract as a whole. If it is to exclude liability for negligence, it must be most clearly and unambiguously expressed, and, in such a contract as this, must be construed *contra proferentem.* I do not think that there is any doubt so far. But I venture to add one further qualification, or at least clarification: one must not strive to create ambiguities by strained construction, as I think the appellants have striven to do. The relevant words must be given, if possible, their natural, plain meaning. Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion; this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives and possibly also the opportunity of the other party to insure.[145]

This passage was quoted with approval by Lord Denning in his Court of Appeal judgment in the *Finney Lock Seeds* case.[146]

Lord Fraser emphasized the distinction between the exclusion clauses and clauses merely limiting liability:

> There are later authorities which lay down very strict principles to be applied when considering the effect of clauses of exclusion or of indemnity: see particularly the Privy Council case of *Canada Steamship Lines Ltd. v. R.* . . . where Lord Morton, delivering the advice of the Board summarised the principles in terms which have recently been applied by this House in *Smith v. UMB Chrysler (Scotland) Ltd.* . . . . In my opinion these principles are not applicable in their full rigour when considering the effect of conditions merely limiting liability. Such conditions will of course be read *contra proferentem* and must be clearly expressed, but there is no reason why they should be judged by the specially exacting standards which are applied to exclusion and indemnity clauses. The reason for imposing such standards on these conditions is the inherent improbability that the other party to a contract including such a condition intended to release the *proferens* from a liability that would otherwise fall on him. But there is no such high degree of improbability that he would agree to a limitation of the liability of the *proferens*, especially when, as explained in condition 4(i) of the present contract, the potential losses that might be caused by the negligence of the *proferens* or its servants are so great in proportion to the sums that can reasonably be charged for the services contracted for. It is enough in the present case that the condition must be clear and unambiguous.[147]

Lord Fraser's formulation of the distinction between exclusion and limitation clauses was quoted with approval by the House of Lords in the *Finney Lock Seeds* case.[148] However, Lord Denning in his Court of Appeal judgment in the same case,[149] referred to what Lord Sumner said fifty years ago: "There is no difference in principle between words

[145] *Supra* note 143, at 102–03, [1983] 1 W.L.R. at 966.
[146] [1983] 1 Q.B. 284, at 296, [1983] 1 All E.R. 108, at 113 (C.A. 1982).
[147] *Supra* note 143, at 105–06, [1983] 3 W.L.R. at 970.
[148] *Supra* note 144, at 741, [1983] 3 W.L.R. at 168 (Lord Bridge).
[149] *Supra* note 146, at 301, [1983] 1 All E.R. at 116. *See also* text at note 173 *infra.*

which save them from having to pay at all and words which save them from paying as much as they would otherwise have had to pay."[150]

Canada Steamship Lines Ltd. v. The King,[151] referred to by Lord Fraser, contains a well-known passage by Lord Morton, summarizing the principles to be applied in determining whether an exemption clause extends to the liability for negligence. In *Finney Lock Seeds*, Kerr L.J. paraphrased this passage as follows:

> (1) If the contract contains an express exemption from the consequence of negligence for which the party in default would otherwise be responsible, then effect must be given to it. (2) If there is no express reference to negligence, then the court must consider whether the words used are nevertheless wide enough, in their ordinary meaning, to cover loss or damage due to negligence; but any doubt in this connection must be resolved against the defaulting party. (3) However, even if the words used are wide enough for this purpose, the court must consider whether liability for the loss or damage in question may arise on some ground other than that of negligence, which ground is not so fanciful or remote that the party in default cannot be supposed to have desired protection against it.[152]

Lord Fraser, who expressed the view that these principles are not applicable in their full rigour in limitation clauses,[153] held that the limitation clause in *Ailsa Craig* referring to "[a]ny liability. . . whether under the express or implied terms of this Contract or at Common Law, or in any other way" extended to negligence. Lord Fraser explained further that liability at common law is undoubtedly wide enough to cover liability including the negligence of the *proferens* himself.[154]

The judgment of the House of Lords in *Ailsa Craig* may be summarized as follows:

1. The effectiveness of an exemption clause is a question of construction and must be decided in the context of the contract as a whole.[155]
2. The words must be given their plain natural meaning and one must guard against strained construction.[156]
3. Distinction should be made between clauses limiting liability and clauses excluding liability. The limitation clauses are not to be construed as rigidly as total exclusionary clauses.[157]
4. The clauses limiting or excluding liability must be construed *contra proferentem*.[158]
5. The principles for determining whether a clause includes liability for negligence, summarized in *Canada Steamship Lines Ltd. v. The*

---

[150] Atlantic Shipping and Trading Co. v. Louis Dreyfus & Co., [1922] 2 A.C. 192, [1922] 1 All E.R. Rep. 559, at 563 (H.L.).

[151] [1952] A.C. 192, [1952] 1 All E.R. 305 (P.C.).

[152] *Supra* note 146, at 312, [1983] 1 All E.R. at 124–25.

[153] *Supra* note 143, at 105–06, [1983] 1 W.L.R. at 970.

[154] *Id.* at 107, [1983] 1 W.L.R. at 972.

[155] *See* text at note 145 *supra*.

[156] *Id.*

[157] *Id.* and *see* text at note 147 *supra* (Lord Fraser).

[158] *Id.*

King[159] and applied in *Smith v. UMB Chrysler (Scotland) Ltd.*[160] were approved, but should not be applied rigidly.[161]

Lords Wilberforce and Fraser found the limitation clause to be clear and unambiguous, and therefore the liability of the Securicor company was effectively limited. In addition, Lord Fraser expressly found that the limitation clause covered negligence.[162] Lords Elwyn-Jones, Salmon and Dowry concurred with both judgments.

The *Finney Lock Seeds* case[163] provided the Court of Appeal and the House of Lords with an opportunity to analyze the impact of the two *Securicor* cases.[164] The facts are simple. Seed merchants supplied seeds which were totally different from those ordered and which proved to be unmerchantable. The defect was not obvious. The farmers planted the seeds and suffered damages of some £100,000. The seed merchants claimed the protection of an exemption clause. The exemption clause was one of long standing in the seed trade and was very wide. It provided for the replacement of defective seeds or the refund of money, but excluded all liability for any loss or damage arising from the use of the seed, for any consequential loss and for any other loss or damage whatsoever.

Two issues were involved. The first, the common law issue, was whether the clause on its true construction was effective to limit the liability of the seed merchants to the refund of the price of the seeds. The second issue, the statutory one, was whether, if the common law issue was decided in favour of the seed merchants, they were nevertheless precluded from relying on this limitation under the provisions of the modified section 55 of the Sale of Goods Act 1979,[165] which states that in a contract of sale of goods, any term is not enforceable to the extent that it is shown that it would not be fair or reasonable to permit reliance on the term. This second issue is of no relevance in Canada, as none of the provincial Sale of Goods Acts contains provisions similar to the amended section 55 of the United Kingdom Act.

The trial judge, Parker J., held that the exemption clause did not cover the breach on the ground that what was delivered was fundamentally different from what was ordered.[166] This reasoning did not find favour with the Law Lords. Lord Diplock commented that Parker J. placed a strained and artificial meaning[167] on the exemption clause. Lord Bridge criticized the reasoning of Parker J., and that of Oliver L.J. in the Court of Appeal, as coming "dangerously near to reintroducing by the back door the doctrine of 'fundamental breach', which this House in the

---

[159] *Supra* note 151.
[160] [1978] 1 All E.R. 18, [1978] 1 W.L.R. 165 (H.L. 1977).
[161] *See* text at note 147 *supra* (Lord Fraser).
[162] *See* text at note 154 *supra.*
[163] *Supra* note 146.
[164] *Supra* note 144.
[165] U.K. 1979, c. 54.
[166] [1981] 1 Lloyd's Rep. 476 (Q.B.).
[167] *Supra* note 144, at 739, [1983] 3 W.L.R. at 165.

Photo Production case had so forcibly evicted from the front."[168]

The Court of Appeal unanimously upheld the trial judgement, but different reasons were put forward.[169] Lord Denning decided the common law issue in favour of the seed merchants, whilst Lords Oliver and Kerr held that the clause did not cover the breach. The Court of Appeal, however, was unanimous in deciding the statutory issue against the seed merchants, as it would not be fair or reasonable to allow them to rely on the clause.

Lord Denning, in his unique style, first traced the history of the judicial approach to exemption clauses.[170] The first phase, some fifty years ago, was *the heyday of freedom of contract*, when the exemption clauses were upheld in the name of freedom of contract. There followed the phase of *the secret weapon*, when the judges tried to curb the excesses by means of the "true construction" of the contracts, whereby the applicability of the exemption clauses was restricted. The *fundamental breach* phase approach was based on the theory that an exemption clause could not be relied upon in a case of fundamental breach, where the breach went to the very root of the contract or where there has been a total failure of consideration. Lord Denning observed that a mistake was made by elevating the concept into a "rule of law". It should have been used as a secret weapon, a rule of construction, by implying that on the true construction of the contract the exemption clause did not avail the party who was guilty of the fundamental breach. *The change of climate* since 1969 was brought about by the reports of the Law Commission, changes in statutory law and the decision in the *Photo Production* case. The exemption clause is now subject to the test of reasonableness. Lord Denning described the effect of the changes as follows:

> What is the result of all this? To my mind it heralds a revolution in our approach to exemption clauses; not only where they exclude liability altogether but also where they limit liability; not only in the specific categories in the Unfair Contract Terms Act 1977, but in other contracts too. Just as in other fields of law we have done away with the multitude of cases on "common employment", "last opportunity", "invitees" and "licensees" and so forth, so also in this field we should do away with the multitude of cases on exemption clauses. We should no longer have to go through all kinds of gymnastic contortions to get round them. We should no longer have to harass our students with the study of them. We should set about meeting a new challenge. It is presented by the test of reasonableness.[171]

Lord Denning then dealt with the impact of the two *Securicor* cases. In his view the first case made it clear that the doctrine of fundamental breach was no longer applicable and was replaced by the test of reasonableness. He supported the proposed test of reasonableness[172] by various *dicta* from the *Photo Production* case. *Ailsa Craig* made a distinction

---

[168] *Id.* at 741, [1983] 3 W.L.R. at 168.
[169] *Supra* note 146.
[170] *Id.* at 296–99, [1983] 1 All E.R. at 113–15 (emphasis added).
[171] *Id.* at 299, [1983] 1 All E.R. at 115.
[172] *Id.* at 300, [1983] 1 All E.R. at 116–17.

between clauses which excluded liability altogether and those which only limited liability. The exclusion clauses are to be construed strictly *contra proferentem* whilst the limitation clauses are to be construed naturally. According to Lord Denning, this must be so because a limitation clause is more likely to be reasonable than an exclusion clause. If one uses a plain natural meaning, there is no difference in principle between them, and Lord Denning referred to a remark to that effect made by Lord Sumner in *Atlantic Shipping and Trading Co. v. Louis Dreyfus & Co.*[173] Lord Denning stated further that it would appear that the House of Lords decision in *Ailsa Craig* was really based on the reasonableness of the limitation clause.[174]

The proposed new test of reasonableness in determining the applicability of the exemption clauses was mentioned several times by Lord Denning in *Finney Lock Seeds.*[175] However, neither Lord Oliver nor Lord Kerr, who sat with Lord Denning on this appeal, referred to the test of reasonableness in their judgments, nor did Lords Diplock and Bridge, who delivered their judgments in the subsequent appeal to the House of Lords. Lord Denning tried to support his test by reference to various passages in the *Photo Production* case. However, these references are not very convincing, since none of the passages referred to suggest the test of reasonableness. There are only isolated expressions such as "a reasonable provision", "nothing unreasonable", "nobody could consider it unreasonable" and "reasonable businessmen", but no clearly defined or applied test of reasonableness.[176]

Dealing with the common law issue, Lord Denning stated that before the decisions of the House of Lords in the two *Securicor* cases, he would have been "hostile" to the clause and he would have said that the goods supplied were different *in kind* from those that were ordered and therefore the seed merchants could not avail themselves of the limitation clause. This approach is no longer available and effect must be given to the natural meaning of the clause. Lord Denning quoted with approval Lord Wilberforce in the *Ailsa Craig* case where he said that "one must not strive to create ambiguities by strained construction" and that "words must be given, if possible, their natural, plain meaning."[177] Here, the merchants did deliver seeds and the limitation clause limited their liability in respect of the seeds supplied. Having decided the common law issue in favour of the merchants, His Lordship held on the statutory issue, that it would not be fair or reasonable to allow the seed merchants to rely on the clause to limit their liability.[178]

Lord Oliver analyzed the *Suisse Atlantique* case and the two *Securicor* cases and stated the following propositions which emerge from this triology of cases:

---

[173] *Id.* at 301, [1983] 1 All E.R. at 116 (Lord Denning M.R.). *See also supra* note 150.
[174] *Id.*
[175] *Id.* at 299–301, [1983] 1 All E.R. at 115–17.
[176] *Id.* at 299–301, [1983] 1 All E.R. at 115–16.
[177] *Supra* note 143, at 102, [1983] 1 W.L.R. at 965–66.
[178] *Supra* note 146, at 295–96, 301–02, [1983] 1 All E.R. at 112–13, 116–17.

(1) There is no rule of law that the effect of a fundamental breach of contract, whether or not accepted by the innocent party as a repudiation, is to preclude reliance on an exclusion clause in the contract inserted for the protection of the party in breach.

(2) The effect of an exclusion clause has to be ascertained simply by construing the contract as a whole. What has to be determined is whether, as a matter of construction, the clause applies to excuse or limit liability for the particular breach which has occurred, whether "fundamental" or otherwise.

(3) There is a presumption that any breach of the primary obligations of the contract will result in continuing secondary obligation on the party in breach to pay compensation for the breach. A clause in the contract excluding, modifying or limiting that secondary obligation is, therefore, to be construed restrictively and *contra proferentem.* (I add in parenthesis that, with deference to Lord Denning M.R., I find the analysis adopted by Lord Diplock in the *Photo Production* case a helpful one, so long as it is borne in mind that the purpose of a contract is performance and not the grant of an option to pay damages.)

(4) The contract has to be construed as a whole, for the exclusion clause is part of an entire contract and may, as a matter of construction, be an essential factor in determining the extent of the primary obligation. Thus, for instance, the *Photo Production* case was not a case of a clause excluding liability for a fundamental breach of the contract but of a clause which, on its true construction, demonstrated that there had been no breach at all of the primary obligation, which was simply to exercise reasonable care.

(5) Since such clauses may not only modify or limit the secondary obligation to pay damages for breach but may also show the extent of the primary obligation, a clause totally excluding liability tends to be construed more restrictively than a clause merely limiting damages payable for breach, for a total exclusion of liability, if widely construed, might lead to the conclusion that there was no primary obligation at all and thus no contract. This is to say no more than that, when it is called on to construe a commercial document clearly intended by both parties to have contractual force, the court will lean against a construction which leads to an absurdity.

(6) Where the language used is unclear or susceptible fairly of more than one construction, the court will construe it in the manner which appears more likely to give effect to what must have been the common intention of the parties when they contracted. But, where, even construing the contract *contra proferentem* and allowing for the presumption of the continuance of a secondary obligation to pay damages for breach of the primary contractual duty, the language of the contract is clear and is fairly susceptible of only one meaning, the court is not entitled to place on an exclusion clause a strained construction for the purpose of rejecting it.[179]

On the common law issue, Oliver L.J. held, after analyzing the clause, that it would be making commercial nonsense to suggest that the parties intended the clause to operate in the circumstances of this case and he further agreed with Kerr L.J. that the merchants were negligent and there was nothing in the clause to protect them from their negligence.[180] Having thus decided the common law issue against the merchants, it was not necessary to deal with the statutory issue, but Oliver L.J. stated that, if

[179] *Id.* at 303–04, [1983] 1 All E.R. at 118–19.
[180] *Id.* at 306, [1983] 1 All E.R. at 120.

necessary, he would be prepared to hold "that reliance on the clause. . . would not be fair and reasonable".[181]

Lord Kerr observed that *Photo Production* laid to rest the doctrine of fundamental breach and that it does not survive under the guise of a rule of construction. His Lordship stated that the principle, put forward in *Ailsa Craig*, that clauses which provide for total exclusion are to be construed more strictly than limitation clauses, is only a guideline to construction.[182]

Following these guidelines, and also applying the principles laid down by Lord Morton in *Canada Steamship Lines Ltd. v. The King*,[183] Kerr L.J. held that the breach could not have arisen without negligence and there was nothing in the clause which would protect the merchants against their own negligence. On the statutory issue, Kerr L.J. held that it would not be fair or reasonable to allow the merchants to rely on the clause.[184]

On further appeal to the House of Lords, the decision of the Court of Appeal was affirmed.[185] The opinion of the House was delivered by Lord Bridge with whom Lords Diplock, Scarman, Roskill and Brightman concurred.

Lord Bridge set out the two issues, one common law and the other statutory, and in dealing with the common law issue, first made reference to the two *Securicor* cases. In his words:

> The *Securicor 1* case gave the final quietus to the doctrine that a "fundamental breach" of contract deprived the party in breach of the benefit of clauses in the contract excluding or limiting his liability. The *Securicor 2* case drew an important distinction between exclusion and limitation clauses.[186]

He then expressed an opinion that the judgments of the trial judge and of Oliver L.J. in the Court of Appeal came dangerously close to reintroducing by the back door the doctrine of "fundamental breach". The trial judge had discussed what Lord Bridge called the "peas and beans" cases, those in which it has been held that exemption clauses do not apply when there has been a contract to sell one thing and quite another thing has been delivered. This was not the case here, since the contract refers to seeds and seeds were sold and delivered. Lord Oliver arrived at the conclusion that the exemption clause was applicable only where the seeds supplied were of the correct description but defective in quality. According to Lord Bridge, this conclusion can only be arrived at by the process of "strained construction" disapproved of in the two *Securicor* cases. The relevant clause, read as a whole, unambiguously limits the liability to replacement of the seeds or refund of the price. Lord Bridge also disagreed with Kerr L.J. (with whose reasoning Oliver L.J. concurred), that the exemption clause did not cover negligence. His

[181] *Id.* at 308, [1983] 1 All E.R. at 124.
[182] *Id.* at 309–10, [1983] 1 All E.R. at 122–23.
[183] *Supra* note 151, at 208, [1952] 1 All E.R. at 310. *See also* text at note 152 *supra*.
[184] *Supra* note 146, at 312–13, [1983] 1 All E.R. at 124–25.
[185] *Supra* note 144.
[186] *Id.* at 741, [1983] 3 W.L.R. at 168.

conclusion was that the exemption clause unambiguously limited the liability, and there is no principle of construction which can properly confine the clause to breaches arising without negligence.[187]

Having decided the common law issue in favour of the appellant seed merchants, Lord Bridge, dealing with the statutory issue, concurred with the unanimous decision of the Court of Appeal that "it would not be fair or reasonable to allow the appellants to rely on the contractual limitation of their liability."[188]

Lord Diplock, in his brief opinion, concurred with Lord Bridge. He stressed the dangers of placing on the language of the exemption clause a strained and artificial meaning and he repeated Lord Denning's view that:

> [T]he passing of the Supply of Goods (Implied Terms) Act 1973 and its successor, the Unfair Contract Terms Act 1977, had removed from judges the temptation to resort to the device of ascribing to the words appearing in exemption clauses a tortured meaning so as to avoid giving effect to an exclusion or limitation of liability when the judge thought that in the circumstances to do so would be unfair.[189]

The following conclusions may be drawn from the two *Securicor* cases and the *Finney Lock Seeds* case:

1. Exemption clauses should be given effect according to their plain, natural meaning and strained, tortured construction to prevent their application is to be avoided. In this respect, the law may have gone the full circle, back to "the heyday of the freedom of contract".
2. It is unlikely that Lord Denning's proposed test of reasonableness will be followed, except perhaps as a general guide of construction as to what is a reasonable interpretation of the exemption clause, but this has always been a general rule of construction.
3. The effect of the distinction between the total exclusionary and limitation clauses, proposed in *Ailsa Craig*, is difficult to assess. The purpose of the distinction is to provide a less strict interpretation of the limitation clauses. If this is done, then a modification is grafted on the rule of giving the exemption clauses their plain, natural meaning. You cannot have both at the same time. In principle and in effect, there is no real difference between a clause which excludes a liability altogether and a clause which limits it to, say, $200, or, as in the *Finney Lock Seeds* case, to 0.33% of the damage suffered. It is submitted that this distinction is not well founded.

In Canada, although the courts have not analyzed the exemption clauses in as great a depth as their United Kingdom counterparts have, some recent decisions indicate that the courts will uphold exemption

---

[187] *Id.* at 740–42, [1983] 3 W.L.R. at 169.

[188] *Id.* at 744, [1983] 3 W.L.R. at 172.

[189] *Id.* at 739, [1983] 3 W.L.R. at 165–66. There is no similar legislation in Canada. As this was probably Lord Denning's last judgement before the Appellate Committee of the House of Lords, Lord Diplock used this opportunity to pay a tribute to Lord Denning's unique and eminently readable style of exposition and his outstanding contribution to the development of the common law.

clauses which are clear and unambiguous, even if there has been negligence or fundamental breach. In *Delaney v. Cascade River Holidays Ltd.*,[190] Mr. Justice Callaghan of the British Columbia Supreme Court upheld a clear and unambiguous exemption clause, even though he found negligence and fundamental breach. The deceased was a passenger on a white water rafting expedition conducted by the defendant. The raft overturned and as the lifejacket was inadequate, the passenger drowned. The operator was negligent in providing inadequate life-saving devices. The plaintiff widow brought an action in contract for an alleged breach and in tort for negligence. The Court held that the liability release form signed by the deceased prior to the excursion relieved the defendant from liability. The defendant took reasonable steps to bring the exemption clause to the notice of the deceased. The clause exempted the defendants from liability from any loss or damage in connection with the expedition for any reason whatsoever, including negligence of the defendant, his agents or servants.

In *Craven v. Strand Holidays (Canada) Ltd.*,[191] the respondents were injured while travelling in a bus. The bus travel was part of a package tour arranged by the tour operators. The respondents brought an action in contract and tort against the operators, alleging breach of an implied term of safe passage and negligence. The Court found that there was no breach of any express or implied term of the contract and no liability in tort for negligence. There was an exemption clause in the contract which provided that the defendants were not responsible for acts or omissions of other suppliers, which would relieve the tour operator from liability for the negligence of the bus driver. The trial judge, relying on *Tilden Rent-A-Car Co. v. Clendenning*,[192] found that the clause was ineffective as it was not brought to the proper attention of the respondents. The Ontario Court of Appeal distinguished the *Tilden* case. This was not a case where the respondents accepted a standard form contract containing onerous conditions in small print under circumstances where no one could be expected to read it.

C. *Collateral Contracts and Negligent Misrepresentations*

1. *Collateral Contracts*

The development of the concepts of collateral contracts and negligent misrepresentation (the *Hedley Byrne*[193] doctrine), is a continuing process and has contributed greatly to the development of the law of contracts in general. These concepts have freed contract law from the shackles of nineteenth century formalism, which insisted that written contracts

[190] 34 B.C.L.R., 16 Bus. L.R. 114 (S.C. 1981).
[191] 40 O.R. (2d) 186, 142 D.L.R. (3d) 31 (C.A. 1981).
[192] 18 O.R. (2d) 601, 83 D.L.R. (3d) 400 (C.A. 1978).
[193] Hedley Byrne & Co. v. Heller & Partners Ltd., [1964] A.C. 465, [1963] 2 All E.R. 575 (H.L. 1963).

were sacrosanct, and that oral statements could create a liability only when solemnly affirmed at the time of making a contract. These concepts also brought contracts closer to the everyday reality of business life and provided for more just, realistic and common sense determinations of obligations arising between the parties to commercial transactions.

The scope of this paper does not permit a comprehensive examination of these concepts and of the closely related doctrine of parol evidence. Instead, a broad outline of these concepts will be given and some recent relevant cases will be mentioned.

Collateral contracts are statements which are more than mere representations. They give rise to an entirely separate contract, collateral to but distinct from the main contract, the breach of which gives rise to an action for damages. Such a contract may arise quite independently of the main contract in a tripartite situation, for example where a representor (such as a manufacturer) induces a prospective buyer to buy his product from a third party (such as a retailer),[194] or it may be merely an adjunct to the main contract between two parties. In this latter situation there is really no need to speak about the warranty as collateral, as suggested by Lord Denning in *Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd.*[195]

The concept of collateral contract was stated by Lord Moulton in the often quoted passage:

> 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. But such collateral contracts must from their very nature be rare. The effect of a collateral contract such as that which I have instanced would be to increase the consideration of the main contract by £100, and the more natural and usual way of carrying this out would be by so modifying the main contract and not by executing a concurrent and collateral contract. *Such collateral contracts*, the *sole effect* of which is to vary or add to the terms of the principal 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.[196]

Collateral contracts have been found to exist in a large number of English and Canadian cases.[197] Their effects may be observed in the following three different situations.

---

[194] *E.g.*, the representor could be a manufacturer and the third party a retailer. *Cf.* Shanklin Pier Ltd. v. Detel Products Ltd., [1951] 2 K.B. 854, [1951] 2 All E.R. 471.

[195] [1965] 2 All E.R. 65, [1965] 1 W.L.R. 623 (C.A.).

[196] Heilbut, Symons & Co. v. Buckleton, [1913] A.C. 30, at 47, [1911–13] All E.R. Rep. 83, at 90–91 (H.L. 1912) (emphasis added).

[197] *See, e.g.*, Murray v. Sperry Rand Corp., 23 O.R. (2d) 456, 5 Bus. L.R. 284 (H.C. 1979); Sodd Corp. v. Tessis, 17 O.R. (2d) 158, 79 D.L.R. (3d) 632 (C.A. 1977); Esso Petroleum v. Mardon, [1976] Q.B. 801, [1976] 2 All E.R. 2 (C.A.); Ford Motor Co. v. Haley, [1967] S.C.R. 437, 62 D.L.R. (2d) 329, *aff'g, sub nom.* Traders Finance Co. v. Haley, 57 D.L.R. (2d) 15 (Alta. C.A. 1966); Wells (Merstham) Ltd. v. Buckland Sand and Silica Ltd., [1965] 2 Q.B. 170, [1964] 1 All E.R. 41 (1963).

They create a new head of liability, as in tripartite agreements, where a representor becomes liable in respect of a statement inducing a promisee to enter into a contract; a typical example being the liability of a manufacturer for statements inducing purchasers to buy his products from a retailer.[198]

They convert a representation into a warranty, for example a statement which is not incorporated into a contract is treated as an independent warranty.[199]

They override the terms of the main contract, especially exemption clauses.[200]

It is inevitable that the concept of collateral contracts clashes with the rule of parol evidence. The rule of parol evidence states that where there is a written contract, parol (or extrinsic) evidence is inadmissible to contradict the terms of the written contract. Yet it is the very nature of collateral contracts that they supplement, change or contradict the terms of the main contract, and it frequently happens that the main contract is in writing whilst the collateral contract is an oral assertion. English courts invariably rule that the collateral contracts prevail over the terms of the main contracts and disregard the rule of parol evidence. Thus, in *Couchman v. Hill*, Scott L.J. held "there was clearly an oral offer of a warranty which overrode the stultifying condition in the printed term. . .".[201] A similar decision was reached in *Harling v. Eddy*, where Sir Raymond Evershed, M.R. quoted with approval the above statement of Scott L.J.,[202] and Denning L.J. stated: "In my opinion, the law is that if a seller of goods by auction gives an express oral warranty, he cannot escape from his responsibility for it by saying that the catalogue contained an exempting clause."[203] Although these two cases concern sales by auction, there is no reason why these *dicta* should not have general application. A definite pronouncement on the conflict between collateral contracts and parol evidence was made in *Mendelssohn v. Normand Ltd.*, where Lord Denning stated:

> Such a statement is binding on the company. It takes priority over any printed condition. There are many cases in the books when a man has made, by word of mouth, a promise or a representation of fact, on which the other party acts by entering into the contract. In all such cases the man is not allowed to repudiate his representation by reference to a printed condition, see *Couchman v. Hill* [1947] K.B. 554; *Curtis v. Chemical Cleaning and Dyeing Co.* [1951] 1 K.B. 805; and *Harling v. Eddy* [1951] 2 K.B. 739; nor is he allowed to go back on his promise by reliance on a written clause, see *City and*

[198] *Cf.* cases cited note 197 *supra.*

[199] *Cf.* Murray v. Sperry Rand Corp., *supra* note 197; Sodd Corp. v. Tessis, *supra* note 197; Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd., *supra* note 195; Harling v. Eddy, [1951] 2 K.B. 739, [1951] 2 All E.R. 212 (C.A.); Couchman v. Hill, [1947] K.B. 554, [1947] 1 All E.R. 103 (C.A. 1946); Hopkins v. Tanqueray, 15 C.B. 139, 139 E.R. 369 (C.P. 1854).

[200] *Cf.* Mendelssohn v. Normand, *supra* note 137; Harling v. Eddy, *supra* note 199; Couchman v. Hill, *supra* note 199.

[201] Couchman v. Hill, *supra* note 199, at 558, [1947] 1 All E.R. at 105.

[202] Harling v. Eddy, *supra* note 199, at 744, [1951] 2 All E.R. at 216.

[203] *Id.* at 746, [1951] 2 All E.R. at 217.

> *Westminster Properties (1934) Ltd. v. Mudd* [1959] Ch. 129, 145 by Harman J. The reason is because the oral promise or representation has a decisive influence on the transaction — it is the very thing which induces the other to contract — and it would be most unjust to allow the maker to go back on it. The printed condition is rejected because it is repugnant to the express oral promise or representation. As Devlin J. said in *Firestone Tyre and Rubber Co. Ltd. v. Vokins & Co. Ltd.* [1951] 1 Lloyd's Rep. 32, 39: "It is illusory to say: 'We promise to do a thing, but we are not liable if we do not do it'." To avoid this illusion, the law gives the oral promise priority over the printed clause.[204]

Lord Justice Phillimore in the same case expressed a similar view:

> Whether you regard that promise as a representation or whether you regard it as a collateral term of the contract, or whether you regard the contract as being oral and partly in writing in the shape of the ticket, it seems to me it can make no real difference.[205]

This attitude of the English courts is in accordance with the present commercial practice, where great reliance is placed on verbal undertakings and the written contract is frequently looked upon as not amounting to more than a formal necessity or perhaps even a nuisance. The reasoning of *Mendelssohn v. Normand Ltd.* has found favour in a number of Canadian cases.[206]

There is, however, the controversial decision in *Hawrish v. Bank of Montreal*,[207] where the Supreme Court of Canada adopted a strict formalistic attitude, holding that a collateral agreement cannot be established where it is inconsistent with or contradicts the written agreement. This decision was followed on this point in *Bauer v. Bank of Montreal*,[208] and in *Carman Construction Ltd. v. C.P.R.*,[209] both Supreme Court of Canada decisions.

Two recent decisions dealing with collateral contracts should be briefly examined because of their impact. In *Esso Petroleum Co. v. Mardon*,[210] an English Court of Appeal case, a service station operator entered into a contract for lease of a service station, relying on a statement by the lessor, a petroleum company, about the "estimated annual consumption" of petrol. This statement was made negligently and the actual consumption was well below the estimate. Lord Denning (Ormrod and Shaw L.J.J. delivering concurring judgments) held that the statement constituted both a collateral contract and a negligent misrepresentation under the *Hedley Byrne* doctrine.

---

[204] *Supra* note 139, at 183–84, [1969] 2 All E.R. at 1218.

[205] *Id.* at 186, [1969] 2 All E.R. at 1220.

[206] *See, e.g.*, Findlay v. Couldwell, [1976] 5 W.W.R. 340, 69 D.L.R. (3d) 320 (B.C.S.C.); J. Evans & Sons (Portsmouth) Ltd. v. Andrea Merzario Ltd., [1976] 2 All E.R. 930, [1976] 1 W.L.R. 1078 (C.A. 1975); Canadian Acceptance Corp. v. Mid-Town Motors Ltd., 72 W.W.R. 365 (Sask. Dist. Ct. 1970).

[207] [1969] S.C.R. 515, 2 D.L.R. (3d) 600.

[208] [1980] S.C.R. 102, at 113, 33 C.B.R. (N.S.) 291, at 300.

[209] 18 Bus. L.R. 65, 136 D.L.R. (3d) 193 (1982).

[210] *Supra* note 197.

Murray v. Sperry Rand Corporation is a well reasoned and well researched decision of the Ontario High Court.[211] During the negotiations for the purchase of a forage harvester, a farmer was given a sales brochure issued by the manufacturers. The farmer explained to the dealer and to a representative of the Canadian distributor his type of farming and was given assurances that the machine would perform as described in the sales brochure and would be ideally suited for his type of farming. The machine did not perform — at best it was able to cut and chop sixteen tons per hour although the sales brochure advertised forty-five to sixty tons per hour. Mr. Justice Reid found that the oral statements by the dealer and the distributor and the sales brochure of the manufacturer constituted collateral contracts. In addition, the dealer was liable for breach of implied conditions of fitness and merchantable quality.[212] There was an exemption clause in the contract of sale between the farmer and the dealer. Clearly such a clause could not nullify the collateral warranties of the manufacturer and the distributor, but it could exempt the dealer. Mr. Justice Reid did not have to decide the question of whether a disclaimer clause in the main contract nullifies the collateral warranty, because he found that the representations to the farmer were fundamental to the contract. The failure of the machine went to the root of the contract and the disclaimer clause would not protect against breach of a fundamental term of the contract. This is somewhat circuitous reasoning, but from the subsequent quotations from, and references to, cases it appears that the judge meant that exemption clauses are not available where a breach goes to the root of the contract. It is to be noted that this judgment predates the House of Lords decision in *Photo Production*.[213]

2. *Negligent Misrepresentations*

The concept of negligent misrepresentation, actionable in tort, had its genesis in the House of Lords judgment in *Hedley, Byrne & Co. v. Heller & Partners Ltd.*,[214] although the concept was put forward by Lord Denning, but not approved by the majority of the English Court of Appeal, in *Candler v. Crane, Christmas & Co.*[215] The principle in *Hedley Byrne* is that where a person "possessed of a special skill undertakes, quite irrespective of contract, to apply that skill for the assistance of another person who relies upon such skill, a duty of care will arise. The fact that the service is to be given by means of, or by the instrumentality of, words can make no difference."[216] This concept has been narrowed by the decision of the Privy Council in *Mutual Life v. Evatt*,[217] in which a majority of the Privy Council gave a fairly narrow construction

[211] *Id.*
[212] Sale of Goods Act, R.S.O. 1980, c. 462, subs. 15(1) and 15(2).
[213] *See* text accompanying notes 138 and 139 *supra*.
[214] *Supra* note 193.
[215] [1951] 2 K.B. 164, [1951] 1 All E.R. 426 (C.A.).
[216] *Supra* note 193, at 502–03, [1963] 2 All E.R. at 594 (Lord Morris of Borth-y-Gest).
[217] [1971] A.C. 793, [1971] 1 All E.R. 150 (P.C. 1970) (Aust.).

of the duty of care of people giving advice, restricting liability to professional advice givers. This restrictive interpretation has not been generally followed by courts, for example, the High Court of Australia decision in *Shaddock & Associates v. Paramatta City Council* does not do so.[218]

The concept of *Hedley Byrne* has been applied in a number of cases where a party was induced to enter into a contract by a negligent misrepresentation. In this context doubts were voiced as to whether a tort action is available in a contractual situation. In *J. Nunes Diamonds Ltd. v. Dominion Electric Protection Co.*,[219] the Supreme Court of Canada, in a majority decision delivered by Mr. Justice Pigeon, held that *Hedley Byrne* is inapplicable "where the relationship between the parties is governed by a contract, unless the negligence relied on can properly be considered as 'an independent tort' unconnected with the performance of the contract."[220] Quite apart from the conceptual difficulty of "independent" tort, this decision is contrary to the general principle of law, that liability in contract and tort may exist concurrently, which is discernible in other judgments. In *Esso Petroleum Co. v. Mardon*,[221] it was held that the *Hedley Byrne* principle is applicable between contracting parties and this statement was supported by many precedents. *Esso Petroleum* was followed in the Ontario Court of Appeal decision of *Sodd Corporation v. Tessis*,[222] where the Court held that the *Esso* case was authority for the proposition that a contractual relationship does not preclude a claim in tort under the *Hedley Byrne* doctrine. It would thus appear that in Ontario the question is settled.[223]

The complex problem of collateral contract, negligent misrepresentation, parol evidence and exemption clauses has recently occupied the Supreme Court of Canada in *Carman Construction Limited v. Canadian Pacific Railway Co.*[224] Regrettably, the judgment leaves many questions unanswered. On the facts, C.P.R. invited three firms to tender for the widening of a railway siding. The tender was to be lodged within three days of the invitation. There was not enough time for the bidders to engage a consultant to estimate the volume of overburden to be removed. The president of Carman Engineering therefore called at the C.P.R. district engineer's office, where someone gave him an estimate of volume of overburden. This estimate was erroneous and was given negligently. Carman based its tender on this estimate and was awarded the contract. There was a clause in the contract, of which Carman was fully aware, to the effect that the contractor entered into the contract on his own knowledge of the work to be done and that he did not rely on any

[218] 36 A.L.R. 385 (H.C. 1981).

[219] [1972] S.C.R. 769, 26 D.L.R. (3d) 699.

[220] *Id.* at 777–78, 26 D.L.R. (3d) at 727–28.

[221] *Supra* note 197.

[222] *Id.*

[223] For a more comprehensive treatment, *see* the thorough analysis by Schwartz, *Hedley Byrne and Pre-Contractual Misrepresentations: Tort Law to the Aid of Contract?*, 10 OTTAWA L. REV. 581 (1978).

[224] *Supra* note 209, *aff'g* 124 D.L.R. (3d) 680 (C.A. 1980), *aff'g* 109 D.L.R. (3d) 288 (H.C. 1980).

representations made by the C.P.R. As the estimates were erroneous, Carman brought an action for the additional costs of the removal of the overburden.

The trial judge found that the statements made in the engineer's office amounted to a collateral contract, but that the exemption clause deprived it of any effect.[225] The Ontario Court of Appeal, in a brief judgment, approved of this reasoning.[226] On appeal, the Supreme Court of Canada, speaking through Mr. Justice Martland, delivered a judgment which is extremely formalistic, does not deal fully with the facts of the case and does not address adequately the legal principles involved. The Supreme Court held that no collateral warranty had been established and that the claim for negligent misrepresentation was precluded by the "non-reliance" provision.

So far as the alleged collateral warranty is concerned, the Court found that there was no express warranty. Some passages in the judgment indicate a very rigid and formalistic approach to this question. The Court further found that the non-reliance clause prevented the existence of the collateral warranty. There are many cases where an exemption clause has been held to be nullified by a collateral warranty.[227] It is unfortunate that these cases were not examined and distinguished or explained. Mr. Justice Martland also mentions the parol evidence rule as another ground for denying the existence of the collateral warranty. The Court dogmatically followed *Hawrish v. Bank of Montreal*[228] to the effect that parol evidence cannot contradict a written agreement. No consideration was given to many of the important cases, English or Canadian, holding that an oral clause overrides the written contract.[229]

On the question of negligent misrepresentation, the Supreme Court held that the non-reliance clause prevented the assumption of a duty of care and thus a claim in negligence did not arise.[230]

V. DAMAGES

Some recent Canadian cases dealing with damages should be noted. They underline the modern tendency to take a broader view of contractual

[225] 28 O.R. (2d) 232, 109 D.L.R. (3d) 288 (H.C. 1980).

[226] 33 O.R. (2d) 472, 124 D.L.R. (3d) 680 (C.A. 1981).

[227] *Cf.* Murray v. Sperry Rand Corp., *supra* note 197; Sodd Corp. v. Tessis, *supra* note 197; Mendelssohn v. Normand, *supra* note 137; Dick Bentley Productions Ltd. v. Harold Smith (Motors) Ltd., *supra* note 195; Harling v. Eddy, *supra* note 199; Couchman v. Hill, *supra* note 199.

[228] *Supra* note 146.

[229] *Cf.* Hyndman v. Jenkins, 29 Nfld. & P.E.I.R. 331, 16 C.C.L.T. 296 (P.E.I.S.C. 1981); Bower v. Technical Marketing Assocs. Ltd., 35 N.S.R. (2d) 1 (S.C. 1979); Findlay v. Couldwell, *supra* note 206; J. Evans & Sons (Portsmouth) Ltd. v. Andrea Merzario Ltd., *supra* note 206; Canadian Acceptance Corp. v. Mid-Town Motors Ltd., *supra* note 206; Mendelssohn v. Normand Ltd., *supra* note 137; Harling v. Eddy, *supra* note 199; Couchman v. Hill, *supra* note 199.

[230] For a comprehensive commentary on this case, *see* Hayek, *Collateral Contracts and the Supreme Court of Canada: Carman Construction Ltd. v. Canadian Pacific Railway Co.*, 7 CAN. BUS. L.J. 328 (1982).

relations, to expand the scope of liability and to emphasize the concept of fairness rather than that of commercial certainty.[231]

A. *Damages for Mental Distress*

The principle that damages for mental distress are recoverable where they were reasonably forseeable at the time the contract was entered into has been reiterated in a series of recent decisions. The breakthrough of the orthodox view that damages for injured feelings are not recoverable for breach of contract[232] was the case of *Jarvis v. Swans Tours Ltd.*,[233] an English Court of Appeal decision. This case was applied in Canada in *Newell v. Canadian Pacific Airlines Ltd.*[234] and *Pilon v. Peugeot Canada Ltd.*[235] The whole problem of damages for mental distress and punitive damages was recently extensively canvassed by Mr. Justice Linden in *Brown v. Waterloo Regional Board of Commissioners of Police.*[236] Regarding damages for mental distress, Linden J. stated that they are recoverable if they were within the contemplation of the parties at the time they entered the contract. It is not normally contemplated that mental suffering will result from a breach of an ordinary commercial contract, but where the contract affects "personal, social or family interests", the likelihood of such occurrence may be foreseen.[237] Thus, in contracts of employment, damages for mental distress are recoverable where they were reasonably foreseeable at the time the contract was entered into and if they resulted from the breach of such contract.[238]

Brown v. Waterloo Regional Board of Commissioners of Police was followed in *Grant v. McMillan Bloedel*,[239] *Fulton v. Town of Fort Erie*,[240] *Bohemier v. Storwal International Inc.*,[241] and *Cleary v. Cabletronics Inc.*,[242] where the Courts held that a claim for damages for loss of reputation may be made in an action for damages for wrongful dismissal.

The Ontario Court of Appeal, speaking through Mr. Justice Weatherston, overruled Linden J.'s award of $10,000 for mental suffering. Mr. Justice Weatherston reviewed the development of damages for mental distress, concluding that there may be circumstances where a

---

[231] *Cf.* Grosman & Marcus, *New Developments in Wrongful Dismissal Litigation*, 60 CAN. B. REV. 656 (1982); Swinton, *Foreseeability: Where Should the Award of Contract Damages Cease?*, in STUDIES IN CONTRACT LAW 61 (B. Reiter & J. Swan eds. 1980).

[232] Addis v. Gramophone Co., [1909] A.C. 488, 101 L.T. 466 (H.L.).

[233] Jarvis v. Swans Tours Ltd., [1973] Q.B. 233, [1973] 1 All E.R. 71 (C.A. 1972).

[234] 14 O.R. (2d) 752, 74 D.L.R. (3d) 574 (Co. Ct. 1976).

[235] 29 O.R. (2d) 711, 114 D.L.R. (3d) 378 (H.C. 1980).

[236] 37 O.R. (2d) 277, 136 D.L.R. (3d) 49 (H.C. 1982).

[237] *Id.* at 284, 136 D.L.R. (3d) at 56.

[238] *Id.* at 285, 136 D.L.R. (3d) at 57.

[239] 83 C.L.L.C. para. 14,002 (Ont. H.C. 1982).

[240] 40 O.R. (2d) 235, 142 D.L.R. (3d) 487 (H.C. 1982).

[241] 40 O.R. (2d) 264, 142 D.L.R. (3d) 8 (H.C. 1982).

[242] 39 O.R. (2d) 456, 140 D.L.R. (3d) 110 (H.C. 1982).

breach of contract will give rise to a claim for damages for mental distress, and quoting with approval paragraph 341 of the *Restatement of the Law of Contracts*:

> There is sufficient authority to justify the statement that damages will be awarded for mental suffering caused by the wanton or reckless breach of a contract to render a performance of such a character that the promisor had reason to know when the contract was made that a breach would cause such suffering, for reasons other than pecuniary loss.[243]

Whilst recognizing the appropriateness of the award of damages for mental distress in special circumstances, the Court of Appeal overruled Linden J. on a technical ground that the actions of the Board in dismissing the respondent as a Chief of Police were not actionable.[244] It would thus appear that the main thrust of Linden J.'s judgment, favouring the award of damages for mental distress in certain wrongful dismissal situations, was not affected by the Court of Appeal reversal.

B. *Aggravated and Punitive Damages*

Mr. Justice Linden in *Brown*[245] draws a distinction between aggravated damages, the aim of which is to "soothe a plaintiff whose feelings have been wounded" and are not meant to punish the defendant, and punitive damages, which are intended to punish and deter.[246] His Lordship further stated that the need for aggravated damages was recognized in the *Pilon* case,[247] and that he would have awarded them in the present case, except for the fact that they had already been awarded on the basis of mental distress.

The principle that punitive damages are not awarded for breach of contract[248] has not been observed in several recent cases. In *Nantel v. Parisien*,[249] Mr. Justice Galligan awarded punitive damages for a breach of contract of lease, and in *Brown* Linden J. concluded that punitive damages may be awarded as a deterrent in those rare situations where a contract has been breached in a high-handed, shocking and arrogant fashion.[250] In *Centennial Centre of Science and Technology v. VS Services Ltd.*,[251] a motion to amend pleadings to include a claim for punitive damages in an action for breach of contract was allowed by Mr. Justice DuPont on the ground that "it is impossible that the law may indeed have evolved to the point where punitive damages *ought* now to be awarded in the exceptional case of wilful, wanton, malicious, or other

---

[243] (Unreported, Ont. C.A., 14 Sept. 1983).

[244] *Id.*

[245] *Supra* note 236.

[246] *Id.* at 288, 136 D.L.R. (3d) at 61.

[247] *Supra* note 235.

[248] *See* ANSON'S LAW OF CONTRACT 550 (25th ed. A. Guest 1979); G. FRIDMAN, THE LAW OF CONTRACT 564 (1976).

[249] 18 C.C.L.T. 79, 22 R.P.R. 1 (Ont. H.C. 1981).

[250] *Supra* note 236, at 293, 136 D.L.R. (3d) at 66.

[251] 40 O.R. (2d) 253, 31 C.P.C. 97 (H.C. 1982).

deliberate unconscionable conduct. . .".[252]

C. *Contract and Tort*

A tendency to narrow the distinction between damages in contract and damages in tort is apparent in a number of cases. The established law is that in the case of breach of contract the remoteness of damage must be determined according to the rule laid down in *Hadley v. Baxendale*,[253] which has been interpreted as meaning that the loss must be reasonably contemplated as arising in a great majority of cases. In tort, the test for remoteness is that of foreseeability, which involves a lesser degree of probability.

Dicta attempting to narrow this distinction were made in the *Victoria Laundry* case.[254] In *Koufos v. C. Czarnikow Ltd.*,[255] some of the *dicta* of Asquith L.J. in *Victoria Laundry* were criticized; their Lordships were in agreement that a distinction should be maintained between "likelihood of happening" in contract and "foreseeability of happening" in tort. In *H. Parsons Ltd. v. Uttley Ingham & Co.*,[256] Lord Denning put forward a proposition that in loss of profit cases the test of "reasonable contemplation" that is the contract test, should be maintained, but in physical damage cases the test of "foreseeability", that is the tort test, should be applied. Lords Orr and Scarman were not satisfied that such a distinction was sufficiently supported by the authorities, but expressed views that the distinction between "reasonable contemplation" and "forseeability" is to a great extent semantic only.

This tendency to narrow the gap between contracts and torts is evident in recent literature[257] and in cases discussed above under the headings, Damages for Mental Distress and Aggravated Damages. In *Canlin Ltd. v. Thiokol Fibres Canada Ltd.*,[258] Cory J.A., speaking for the Ontario Court of Appeal, stated that "there is no difference between what a reasonable man might reasonably contemplate and what a reasonable man might reasonably foresee",[259] and referred to the *Parsons* case.[260] This case also confirmed the principle that damages for loss of future profits may be recoverable in an action for a breach of warranty. A number of authorities were reviewed, with the main emphasis placed on *Parsons* and *Sunnyside Greenhouses Ltd. v. Golden West Seeds Ltd.*[261]

---

[252] *Id.* at 256, 31 C.P.C. at 101 (emphasis added).

[253] 9 Ex. 341, 156 E.R. 145 (1854).

[254] Victoria Laundry v. Newman Indus. Ltd., [1949] 2 K.B. 528, [1949] 1 All E.R. 997 (C.A.).

[255] [1969] 1 A.C. 350, *sub nom.* The Heron II, [1967] 3 All E.R. 686 (H.L. 1967).

[256] [1978] Q.B. 791, [1978] 1 All E.R. 526 (C.A. 1977).

[257] *See generally supra* note 231.

[258] 40 O.R. (2d) 687, 142 D.L.R. (3d) 450 (C.A. 1983).

[259] *Id.* at 695, 142 D.L.R. (3d) at 459.

[260] *Supra* note 257.

[261] [1972] 4 W.W.R. 420, 27 D.L.R. (3d) 434 (Alta. C.A.), *aff'd* [1973] 3 W.W.R. 288, 33 D.L.R. (3d) 384 (S.C.C.).