

Practice questions for Chapter 7 – The terms of the contract

Essay question

'The law of contract should aim to provide as much clarity and certainty as possible, but the law relating to the implication of contractual terms is excessively vague and unclear.'

Discuss the validity of this statement.

Introduction

- It is unlikely that even the most carefully drafted contract will be fully complete. The ability of the parties to predict future events is limited, and so most contracts will contain gaps of some kind. If the gaps are too large, the contract will be declared void on the ground of uncertainty, but if the gaps are not too large, the court may fill them by implying terms into the contract.
- This essay will look at when the courts will imply terms and the tests used to determine whether or not terms should be implied. Given that the implication of terms may completely go against the wishes of the parties, it is important that the courts provide clear rules on when terms will be implied. Unfortunately, as we shall see, the rules regarding the implication of terms lack certainty and consistency.

Terms implied in fact

- The court may be of the opinion that the particular facts of a case merit the implication of a term. In such cases, the court will imply a term on the basis that the parties meant to imply such a term, but failed to do so. Accordingly, the implication of terms in fact is based upon the unexpressed wishes of the parties.
- The question arises when should the court imply terms in law. The courts have been unable to devise a single test and, instead, two tests have been established by the courts, namely the 'business efficacy' test and the 'officious bystander' test. Briefly set out how these tests operate and provide a brief case law example.
- The business efficacy test was established in *The Moorcock*,¹ but the application of the test itself can be problematic. Under the test, the courts will only imply a term where implication is necessary to give the contract business efficacy, but it is arguable that there was no need to imply a term in *The Moorcock*. The contract would have been just as valid without the implied term.
- The officious bystander test was established in the case of *Shirlaw v Southern Foundries (1926) Ltd*,² and provides that the court will imply a term if it is 'something so obvious that it goes without saying...' The problem that arises is that what is obvious to one judge might not be so obvious to another.
- Accordingly, neither test is especially clear or certain, and this uncertainty is compounded by the fact that the relationship between the two tests have never been clarified by the court. In the majority of cases, the two tests will produce the same result, but not always. Where the two tests produce differing results, which test should the court apply? The court has provided inconsistent advice.

¹ (1889) LR 14 PD 64 (CA).

² [1939] 2 KB 206 (CA).

- In *Ashmore v Corporation of Lloyd's (No 2)*,³ the High Court stated that satisfying either test will suffice. However, in *Stubbs v Trower Still and King*,⁴ the Court of Appeal stated that both tests must be satisfied. To make matters more confusing, in *Dellacassa and Associates Ltd v Wren Homes Ltd*,⁵ the Court of Appeal merged the two tests and stated that a term would be implied if it would give 'such efficacy to the contract as the parties must have intended, as interpreted by the officious bystander.'
- Clearly, the law in this area is unclear and a definitive higher court ruling is required.

Terms implied in law

- In addition to implying terms in fact, the courts can also imply terms in law. You might want to briefly explain the distinction between the two.
- Terms implied by statute poses no particular problems, but when the term is implied in law by the courts and not by statute, then problems can arise. These problems can be seen in the leading case, namely *Liverpool City Council v Irwin*.⁶ You may want to briefly discuss the facts of the case and the decision of the House. The problem arises in that, whilst the House might have unanimously agreed that a term should be implied, the judges involved could not agree on when terms should be implied in law.
- Lord Cross agreed with Lord Denning in the Court of Appeal and stated that a test of reasonableness should be used. However, Lords Edmund-Davies, Salmon and Wilberforce opined that reasonableness would be insufficient and the test was one of necessity.
- Subsequent cases have indicated that the test of necessity has prevailed,⁷ but the test of necessity is narrower than the test of necessity established in relation to terms implied in fact. As both types of implied term have necessity tests, it has been argued that terms implied in law and terms implied in fact should be better differentiated by having different tests, and that the test used to imply terms in law should be based on reasonableness.⁸ There is evidence that the courts are moving towards a reasonableness test.

In *Crossley v Faithful & Gould*,⁹ Dyson LJ stated that 'rather than focus on the elusive concept of necessity, it is better to recognize that, to some extent at least, the existence and scope of standardized implied terms raise questions of reasonableness, fairness and the balancing of competing policy considerations.' Given such comments, Atiyah has argued that the current standard might be one of reasonable necessity.¹⁰

Conclusion

- The law relating to implied terms does indeed appear to lack clarity. In relation to terms implied in fact, the courts have established two tests, but neither test is wholly certain and the courts have failed to clearly articulate the precise relationship between the two tests and severe inconsistency is evident. Regarding terms in law, similar inconsistency is evident with some judges indicating that the

³ [1992] 2 Lloyd's Rep 620 (QB).

⁴ [1987] IRLR 321.

⁵ 8th December 1982 (CA).

⁶ [1977] AC 239 (HL).

⁷ *El Awadi v Bank of credit and Commerce International SA* [1990] 1 QB 606 (QB).

⁸ See e.g. A Phang, 'Implied Terms in English Law: Some Recent Developments' [1993] JBL 242.

⁹ [2004] EWCA Civ 289.

¹⁰ PS Atiyah, *An Introduction to the Law of Contract* (6th edn, OUP 2006) 161.

relevant test is the test of necessity, but other judges arguing that a test of reasonableness might be more appropriate.

Essay question

Why is it so important for the courts to be able to clearly distinguish between terms and mere representations, and how do the courts determine whether a statement is a term or a mere representation?

Introduction

- Statements made prior to the formation of a contract may become terms of the contract. Should such statements turn out to be untrue or misleading, the recipient of the statement may be able to obtain a remedy for breach of contract. Conversely, statements made may not amount to terms, but may amount to representations. Should a representation be untrue or misleading, no action in breach of contract will lie, but the representee might obtain a remedy by claiming that the statement amounts to a misrepresentation.
- Given the different remedies available for breach of contract and misrepresentation, it is vital that the courts are able to distinguish between statements that amount to terms and statements that amount to mere representations.
- In *Heilbut, Symons & Co v Buckleton*,¹¹ the House of Lords established that, when determining whether a statement is a term or a representation, the courts will look objectively at the words or conduct of the parties in order to determine whether the parties intended for the statement to amount to a term or not. However, this test proved difficult to apply consistently in practice so, to ensure greater consistency, the courts have devised a series of factors that can be taken into account, but it should be noted that these tests are indicative only and are not to be regarded as decisive.

The timing of the statement

- Generally, the longer the time between the making of a statement and the entering into the contract, the less likely it is that the statement will amount to a term. You may want to provide an example of this factor in practice, such as the case of *Bannerman v White*.¹²
- However, this rule is a general one only and, if the evidence indicates so, the courts will hold that a statement amounts to a term even though a lengthy period has passed between the making of the statement and the entering into of the contract.¹³ Similarly, in *Hopkins v Tanqueray*,¹⁴ the court held that a statement amounted to a mere representation even though the statement was made only one day before the contract was entered into.

The importance of the statement

- The more important a statement is to one of the parties, the more likely it is that the statement will constitute a term. If the statement is one that is so important that the representee would not have entered into the contract had the statement not been made, then the statement will almost certainly

¹¹ [1913] AC 30 (HL).

¹² (1861) 10 CBNS 844.

¹³ *Schawel v Reade* [1913] 2 IR 64 (HL).

¹⁴ (1854) 15 CB 130.

constitute a term. The cases of *Bannerman v White*¹⁵ and *J Evans & Son (Portsmouth) Ltd v Andrea Merzario Ltd*¹⁶ provide good examples of this factor in practice.

The knowledge of the parties

- The respective knowledge of the parties is another important factor. A party who has specialist knowledge will be more likely to ascertain the truth of a statement than a party with no knowledge of the topic in question. Accordingly, statements made by parties with specialist knowledge are more likely to be regarded as terms, as can be seen in the case of *Dick Bentley (Productions) Ltd v Harold Smith (Motors) Ltd*.¹⁷ Where the party making the statement has no specialist knowledge, the statement is more likely to amount to a representation, as seen in the case of *Oscar Chess Ltd v Williams*.¹⁸

This factor is especially important in relation to consumer contracts, where the consumer is likely to lack specialist knowledge, whereas the seller is likely to have such specialist knowledge.

Statements of opinion

- Generally, a statement of opinion will not amount to a term or a representation. However, in *Smith v Land and House Property Corporation*,¹⁹ the Court of Appeal held that a statement may amount to a representation where the court is of the opinion that a reasonable man possessing all the knowledge of the representor could not have honestly held such an opinion.
- In limited circumstances, a statement of opinion can even amount to a term, notably where the opinion states a fact that is difficult to verify.²⁰

Statements inviting verification

- If the maker of a statement invites the recipient to verify the validity of the statement. It is unlikely that the statement will amount to a term. The case of *Ecay v Godfrey*²¹ provides a good example of this.
- However, if the maker of the statement specifically states that his statement can be relied upon and that no verification is required, then the statement is likely to amount to a term. The case of *Schawel v Reade*²² demonstrates this in practice.

¹⁵ (1861) 10 CBNS 844.

¹⁶ [1976] 1 WLR 1078 (CA).

¹⁷ [1965] 1 WLR 623 (CA).

¹⁸ [1957] 1 WLR 370 (CA).

¹⁹ (1884) 2 ChD 7 (CA).

²⁰ *Power v Barham* (1836) 4 A&E 473.

²¹ (1947) 80 Ll L Rep 286 (KB).

²² [1913] 2 IR 64 (HL).