



Tenth edition

# Contract Law

Catherine Elliott & Frances Quinn

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Judith Tillson, Senior Lecturer, Staffordshire University

# Contract Law

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# Contract Law

Catherine Elliott and  
Frances Quinn

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# Preface

The tenth edition of this book aims to build on the strengths that have led to the success and popularity of the previous editions, which have been extremely well received by both teachers and students alike. It incorporates all the important legal developments that have taken place since the publication of the last edition. As with our previous editions, our aim has been to provide a clear explanation of the law of contract. As well as setting out the law itself, we look at the principles behind it, and discuss some of the issues and debates arising from contract law. We hope that the material will allow you to enter into some of that debate and develop your own views as to how the law should develop.

One of our priorities in writing this book has been to explain the material clearly, so that it is easy to understand, without lowering the quality of the content. Too often, law is avoided as a difficult subject, when the real difficulty is the vocabulary and style of legal textbooks. For that reason, we have aimed to use 'plain English' as far as possible, and explain the more complex legal terminology where it arises. There is also a glossary explaining common terms at the back of the book. In addition, chapters are structured so that material is in a systematic order for the purposes of both learning and revision, and clear subheadings make specific points easy to locate.

Although we hope that many readers will use this book to satisfy a general interest in the law, we recognise that the majority will be those who have to sit an examination in the subject. Therefore, each chapter features typical examination questions, with detailed guidance on answering them, using the material in the book. This is obviously useful at revision time, but we recommend that, when first reading the book, you take the opportunity offered by the questions sections to think through the material that you have just read and look at it from different angles. This will help you both to understand and to remember it. You will also find that the Appendix at the end of the book gives useful general advice on answering examination questions on contract law.

This book is part of a series that has been produced by the authors. The other books in the series are *English Legal System*, *Criminal Law* and *Tort Law*.

We would like to thank Elliot Schatzberger of Middlesex University for his help in updating this edition.

We have endeavoured to state the law as at 1 January 2015.

**Catherine Elliott and Frances Quinn**  
**London 2015**

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# Introduction

## This chapter discusses:

- why we need contract law;
- the history of contracts;
- the importance of procedural fairness in the development of contract rules;
- the courts' emphasis on looking at the contracting process objectively;
- the impact of the Human Rights Act 1998; and
- the influence of Europe.



Ask most people to describe a contract, and they will talk about a piece of paper – the documents you sign when you start a job, buy a house or hire a television, for example. While it is certainly true that these documents are often contracts, in law the term has a wider meaning, covering any legally binding agreement, written or unwritten. In order to be legally binding, an agreement must satisfy certain requirements (which will be discussed in Part 1) but with a few exceptions, being in writing is not one of those requirements. We make contracts when we buy goods at the supermarket, when we get on a bus or train, and when we put money into a machine to buy chocolate or drinks – all without a word being written down, or sometimes even spoken.

## Why do we need contract law?

The obvious answer is because promises should be binding, but in fact the law only enforces certain types of promise, essentially those which involve some form of exchange. A promise for which nothing is given in return is called a gratuitous promise, and is not usually enforceable in law (the exception is where such a promise is put into a formal document called a deed).

Why then do we need laws specifically designed to enforce promises involving an exchange? The major reason appears to be the kind of society we live in, which is called a market capitalist society. In such a society, people buy and sell fairly freely, making their own bargains, both on the small scale of ordinary shoppers in supermarkets, and on the much bigger one of a project such as the construction of the Channel Tunnel, which involved many different parties, each buying and selling goods and services. Although, as we shall see, there are areas in which government intervenes, in general we choose what we want to buy, who from and, to some extent at least, at what price.

It would be impossible to run a society on this basis if promises were not binding. Long-term projects show this very clearly – contractors working on the Channel Tunnel, for example, would have been very reluctant to invest time and money on the project if they knew that the British and French Governments could suddenly decide that they did not want a tunnel after all, and not be expected to compensate the contractors. On a smaller scale, who would book a package holiday if the tour operator was free to decide not to fly you home at the end of it? How would manufacturers run their businesses if customers could simply withdraw orders, even though the goods had been made specially for them? A market economy will only work efficiently if its members can plan their business activities, and they can only do this if they know that they can rely on promises made to them.

In fact, contract law rarely forces a party to fulfil contractual promises, but what it does do is try to compensate innocent parties financially, usually by attempting to put them in the position they would have been in if the contract had been performed as agreed. This has the double function of helping parties to know what they can expect if the contract is not performed, and encouraging performance by ensuring that those who fail to perform cannot simply get away with their breach.

## The origins of contract law

In order to understand the rationale underlying contract law, it helps to know a little about its history. Although some principles of contract law go back three centuries, the majority of contract rules were established in the early nineteenth century. Before that, contract hardly existed as a

separate branch of law, and took up very few pages in textbooks. Yet today, it is one of the core subjects which lawyers must study, and affects many areas of daily life. What caused the change?

The answer lies in the transformation of our society which occurred during the late eighteenth and early nineteenth centuries, a transformation which has been described as a move from status to contract. Today, we are very used to the important role that 'the market' plays in our society. We take it for granted that, for example, the price of food should generally be set by the manufacturer or retailer, with the customer choosing to take it or leave it. We may not actually negotiate a bargain in many areas of ordinary life, but we see the operation of the market in the fact that manufacturers have to set prices at which people will buy. We would be rather surprised if Parliament suddenly made it illegal to charge more than 50p for a loaf of bread.

Before the nineteenth century, however, there were many areas of life where free negotiation and bargaining were simply not an issue. An example is the market for what were regarded as essential foodstuffs, which included wheat, bread and beer. Although bakers and millers were entitled to make a profit, that did not mean they could sell at whatever price people would pay. Prices and quality standards for bread were fixed, according to the price the baker had had to pay for the wheat, so limiting their profits, and ensuring that they could not take advantage of shortages.

Activities such as buying goods and then selling them in the same market at a higher price, buying up supplies before they reached the market, and cornering the market by buying huge stocks of a particular commodity are all seen as good business practice now, but in the eighteenth-century market for essential foodstuffs, they were criminal offences, called regrating, forestalling and engrossing respectively. The basis for this approach was explained by Kenyon J in **R v Rusby**: 'Though in a status society some may have greater luxuries and comfort than others, all should have the necessaries of life.' In other words, there was a basic right to a reasonable standard of living, and nobody was expected to negotiate that standard for themselves.

A similar, though less humane, approach was taken to relationships between employer and employee – or master and servant, as they were called then. These days, we expect to have an employment contract detailing our hours of work, duties and pay, even though the amount of control we actually have in negotiating those areas may be negligible. In a status society, employment obligations were simply derived from whether you were a master or a servant; masters were entitled to ask servants to do more or less anything, and criminal sanctions could be used against an employee who disobeyed. Employers had obligations too (though rather less onerous than those of employees), which sometimes included supplying food or medical care. Both sets of obligations were seen as fixed for everyone who was either an employee or an employer, and not a matter for individual negotiation. Even wages were often set by local magistrates.

All this began to change in the eighteenth and nineteenth centuries. Society itself was undergoing huge changes, moving from an agricultural to an industrial economy, and with that came political changes, and changes in the way people saw society. With the rise of an economic doctrine called *laissez-faire* came a view that society was no more than a collection of self-interested individuals, each of whom was the best judge of their own interests, and should, as far as possible, be left alone to pursue those interests. If we apply this view to the market for bread, for example, it would suggest that bakers would sell bread for the highest price they could get, while consumers shopped around for the lowest, and the result should be a bargain suitable to both. The market would consist of hundreds and hundreds of similar transactions, with the result that everyone would be able to secure their own best interests, and the state would not need to intervene to do this for them – in fact it should not do so, because the parties should be left alone to decide what was best for them.

This *laissez-faire* approach carved out a very important place for contracts. As we have seen, where people make their own transactions, unregulated by the state, it is important that they keep their promises, and as a result, contract law became an increasingly important way of enforcing obligations.

## Freedom of contract

Its origins in the *laissez-faire* doctrine of the nineteenth century have had enormous influence on the development of contract law. Perhaps the most striking reflection of this is the importance traditionally placed on freedom of contract. This doctrine promotes the idea that since parties are the best judges of their own interests, they should be free to make contracts on any terms they choose – on the assumption that nobody would choose unfavourable terms. Once this choice is made, the job of the courts is simply to act as an umpire, holding the parties to their promises; it is not the courts' role to ask whether the bargain made was a fair one.

Some academics, notably Professor Atiyah (*The Rise and Fall of Freedom of Contract*, 1985), have suggested that this extreme position lasted only a short time, and that the courts were always concerned to establish some concept of fairness. His view has been challenged, but in any case, it is clear that over the last century, the courts have moved away from their reluctance to intervene, sometimes of their own accord, sometimes under the guidance of Parliament through legislation such as the Unfair Contract Terms Act 1977. However, as the basic principle still holds, decisions which actually have their basis in notions of fairness may be disguised behind more technical issues.

## Contract and fairness

Traditional contract law lays down rules which are designed to apply in any contractual situation, regardless of who the parties are, their relationship to each other, and the subject matter of a contract. This means that the law uses basically the same rules to analyse the contract that arises when you go into a supermarket to buy a tin of beans as it does to analyse the contract to build the Channel Tunnel.

The basis for this approach is derived from the *laissez-faire* belief that parties should be left alone to make their own bargains. This, it was thought, required the law simply to provide a framework, allowing parties to know what they had to do to make their agreements binding. This framework was intended to treat everybody equally, since to make different rules for one type of contracting party than for another would be to intervene in the fairness of the bargain. As a result, the same rules were applied to contracts in which both parties had equal bargaining power (between two businesses, for example) as to those where one party had significantly less economic power, or legal or technical knowledge, such as a consumer contract.

This approach, often called procedural fairness, or formal justice, was judged to be fair because it treats everybody equally, favouring no one. The problem with it is that if people are unequal to begin with, treating them equally simply maintains the inequality. This has obvious repercussions in contract law. Take, for example, an employment contract stating that if either party is dissatisfied with the other's performance, the dissatisfied party can terminate the contract at any time. This

clearly amounts to treating both parties in exactly the same way, making them play by the same rules. But in doing so, it gives the more powerful employer the useful opportunity to sack the employee at any time, while the corresponding 'benefit' to the less powerful employee will in many cases amount to no more than the chance to become unemployed.

Over the last century the law has to some extent moved away from simple procedural fairness, and an element of what is called substantive fairness, or distributive justice, has developed. Substantive fairness aims to redress the balance of power between unequal parties, giving protection to the weaker one. So, for example, terms are now implied by law into employment contracts so that employers cannot simply dismiss employees without reasonable grounds for doing so. Similar protections have been given to tenants and to consumers, and in these three areas (and some others) traditional contract rules are overlaid with special rules applying only to particular types of contract. (You can see the way in which this approach operates in Chapter 16.)

The balance between substantive and procedural fairness in contract law is always an uneasy one, but major academics such as Treitel (*The Law of Contract*, 2007) and Atiyah believe that there has been, as Atiyah puts it, 'a move from principle to pragmatism'. He suggests that in modern cases, the courts have been less concerned with laying down general rules, and more with producing justice in individual cases. In fact, an examination of the cases, especially those between businesses, where bargaining power is assumed to be equal, shows that although the courts are often attempting to secure substantive justice, they still tend to hide that attempt behind what appears to be an application of the traditional rules. The cases on innominate terms (p. 145), and on reasonable notice, particularly **Interfoto** (see p. 161), have been seen as examples of this.

## The objective approach

Contract law claims to be about enforcing obligations which the parties have voluntarily assumed. Bearing in mind that contracts do not have to be in writing, and that even where they are, important points may be left out, it is clear that contract law faces a problem: how to find out what – or even whether – the parties agreed. For example, if I promise to clean your car, meaning that I will wash the outside, and you promise to give me £10 in return, assuming that I will vacuum the inside as well, what have we agreed?

Contract law's approach to this problem is to look for the appearance of consent. If my words and/or actions would suggest to a reasonable person that I was agreeing to clean the inside of your car as well as the outside, then that is what I will have to do before I get my £10. This approach was explained by Blackburn J in **Smith v Hughes** (1871): 'If, whatever a man's real intention may be, he so conducts himself that a reasonable man would believe he was assenting to the terms proposed by the other party, and that other party upon that belief enters into the contract with him, the man thus conducting himself would be equally bound as if he had intended to agree to the other party's terms.' This point was repeated by the Supreme Court in **RTS Flexible Systems v Molkerei Alois Müller** (2010) where it stated:

Whether there is a binding contract between the parties and, if so, upon what terms depends upon what they have agreed. It depends not upon their subjective state of mind, but upon a consideration of what was communicated between them by words or conduct, and whether that leads objectively to a conclusion that they intended to create legal relations and had agreed upon all the terms which they regarded or the law requires as essential for the formation of legally binding relations.