Index - Introduction to Contract Law

CHAPTER 1 – INTRODUCTION TO CONTRACT LAW

1. Overview

1.1 A contract is a legally binding promise or agreement. We make contracts on a regular basis without necessarily turning our mind to the fact that we are doing so or the legal consequences – for example, when you order a coffee from your local café, you are entering into a contract to purchase the coffee. Similarly, you might place an online order for groceries or other goods, or purchase an app on your mobile phone, agreeing to the Terms & Conditions as you do so.

1.2 The law of contract governs those every day interactions, as well as far more complex transactions, including purchases of property, commercial transactions and many other types of agreement. Not every agreement will be a binding and enforceable contract. Further, when there is a dispute about a contract, it is not always clear what is included in the terms of the contract.

1.3 Most aspects of contract law are governed by the common law, however an increasing number of statutes (or legislation) also address aspects of contract law.

1.4 This course:

(a) sets out the legal principles relating to the formation of a contract;

(b) considers who are the parties to a contract;

(c) examines the terms of a contract;

(d) discusses vitiating factors, including misleading and deceptive conduct, mistake, duress, undue influence and unconscionability;

(e) explains the law around termination of contracts; and

(f) examines the remedies that might be available when things go wrong.

CHAPTER 2 – FORMATION OF CONTRACT

2. Overview

2.1 There are three principal requirements applicable to all contracts, which will be discussed in turn in this chapter:

(a) Agreement;

(b) Consideration; and

(c) An intention to create legal relations.

2.2 In addition, this Chapter considers contracts requiring written evidence.

3. Agreement

3.1 The first requirement for formation of a contract is an agreement between the parties. This is generally expressed in legal terms as “offer and acceptance”.

3.2 In order for a contract to be binding, it must be possible to identify an offer made by one party and an acceptance of that offer by the other. A contract is said to come into existence when acceptance of an offer has been communicated to the offeror.

3.3 This section will refer to the parties as the *offeror* (the party who makes the offer) and the *offeree* (the party who receives the offer).

How does a Court determine whether there has been offer?

3.4 When considering whether an offer has been made, the Court considers whether there has been an expression of willingness to immediately accept to be bound to the agreement. In other words, an offer indicates the offeror’s intention to immediately be bound to the terms of the offer upon acceptance by the offeree.

3.5 This is based on an objective, not a subjective, assessment of the evidence: it does not matter whether the offeror did *in fact* intend to enter into a contract or to be bound immediately; the offeror will be bound if it would appear to *a reasonable person* in the offeree’s position that the offeror was offering to enter into a contract.

3.6 An offer will not be effective until it has been communicated. It must be sufficiently certain and clearly communicated in order to objectively be understood as an offer.

3.7 An offer may arise in either unilateral or bilateral contracts. A *bilateral contract* is one where the promise is accepted by a counter-promise and the contract creates obligations that each party must perform. A typical example of a bilateral contact is a contract for the sale of goods or performance of services: one party contracts to purchase (and pay for) goods or services, and the other party contracts to provide those goods or services. Both sides of the contracts therefore have obligations that arise under the contract.

Example: *Bilateral contracts*

Sam has purchased a house and wants to do some renovations before moving in. Sam signs a building contract with Kim the builder.

The contract between Sam and Kim is a *bilateral contract*: Kim agrees to build the house and in return, Sam agrees to pay Kim. Both parties have made promises to do certain acts.

3.8 In contrast, a *unilateral contract* is one which can be accepted by the performance of an act. The performance of the act by the offeree creates an obligation on the part of the offeror. For example, a poster on a street pole might advertise a reward for a lost dog. Once the dog is located and returned to its owner, the poster has created an obligation on the part of the offeror to pay the reward. The words on the sign constitute an offer, and the act of finding the dog is the acceptance of the offer.

3.9 It is important to bear in mind that there is a difference between a statement of intention and a promise. For a unilateral contract to arise, the promise must be made in return for the doing of the act. That is, there must be a relation of *quid pro quo* (this for that) between the offeree's act and the offeror's promise. In considering whether a unilateral contract arises, it is useful to consider the following questions:

(a) Has the offeror expressly or impliedly requested the doing of the act by the offeree?

(b) Has the offeror stated a price which the offeree must pay for the promise?

(c) Was the offer made in order to induce the doing of the act?

3.10 Further, a unilateral contract must be contrasted from an *invitation to treat.* In contrast to an offer, which entails an intention to be immediately bound without further discussion or negotiation, an invitation to treat is an invitation to others to make offers or enter into negotiations.

3.11 For example, the display of goods for sale, whether in a shop window or on the shelves of a self-service store, is ordinarily treated as an invitation to treat and not an offer (*Pharmaceutical Society of Great Britain v Boots Cash Chemists (Southern) Ltd* [1953] 1 QB 401). In that case, the contract is not completed until, the customer having indicated what he or she wants, the shopkeeper accepts that offer.

3.12 If the customer taking an item from the shelf and placing it in a basket was to be considered as the acceptance of an offer, the customer would have no right, once having placed an item in a basket, to exchange this item for another.

Case study: *Carlill v Carbolic Smoke Ball Co* [1893] 1 QB 256

The Carbolic Smoke Ball Co produced the 'Carbolic Smoke Ball' designed to prevent users contracting influenza or similar illnesses. The company placed an advertisement in the newspaper that stated that any person who purchased the Smoke Ball and contracted influenza would be entitled to a reward. The advertisement further stated that the company had demonstrated its sincerity by placing £1000 in a bank account to act as the reward.

After seeing this advertisement Mrs Carlill bought one of the balls and used it as directed. She subsequently caught the flu and claimed the reward. The company refused to pay. Mrs Carlill sued for the reward.

The issue for the Court was whether there had been an *offer* or whether the advertisement merely constituted an *invitation to treat.*
The Court held that the advertisement placed by the Carbolic Smoke Ball Co was a unilateral offer. An offer can be made to the whole world, so long as the language used is not too vague to be enforced. Here, the offer was not "mere puff" (i.e. language intended to entice but not to bind the offeree) but demonstrated an intention to be bound upon the offeree accepting the offer by performance of the advertised terms.

3.13 Proposals communicated by electronic means are now the subject of legislation in the *Electronic Transactions Act 1999* (Cth). Section 15B of the Act provides that a proposal to form a contract made through one or more electronic communications that is not addressed to one or more specific parties and is generally accessible to parties making use of information systems is to be considered as an invitation to make offers, unless it clearly indicates the intention of the party making the proposal to be bound in case of acceptance.

Termination of an offer

3.14 An offer may become ineffective or be terminated where (1) there is a lapse of time; (2) the offer is revoked; (3) the offer is rejected; (4); there is a failure of a contingency or condition; or (5) on the death of the offeror or offeree.

Lapse in time

3.15 Where an offer states that it will remain open for a specified period of time, the offer lapses at the end of that period of time without the need for revocation by the offeror.

3.16 Where no time period is specified, the offer will remain open for a reasonable period of time.

Revocation of an offer

3.17 An offer may be revoked at any time before it is accepted. A promise to hold an offer open for a specified period is not generally binding unless the offeree has given consideration for that promise.

3.18 If consideration is given, the promise is considered an option: the option holder is entitled to enter into a contract with the grantor on specified terms, either at a specified time or within a specified period.

3.19 A difficulty arises in determining when an offeror can revoke a unilateral contract. In *Mobil Oil Australia Ltd v Wellcome International Pty Ltd* (1998) 81 FCR 475, the Court held that there is no universal principle that the offeror may not revoke an offer once the offeree embarks upon performance of the act of acceptance.

Rejection of an offer

3.20 Once an offer has been rejected by the offeree, the offer terminates.

3.21 Where an offeree purports to accept an offer, but in fact states terms different to those in the offer, this is considered a *counter-offer.* The making of a counter-offer constitutes an implied rejection of an offer.

Failure of a contingency or condition

3.22 Where the offer is conditional upon a particular condition or event being satisfied, and the condition or contingency is not met, the offer will terminate automatically.

3.23 For example, an offer to sell particular goods may be expressed as being conditional upon the offeror first receiving the goods from a supplier. Where the goods are not received by the offeror, the offer will terminate.

3.24 Alternatively, in the case of construction of a house, an offer by the builder to procure the services of a carpenter may be dependent upon the builder first being awarded the contract for the construction of the house. If that contract does not eventuate, the offer to the carpenter will also terminate.

Death of the offeror or offeree

3.25 As a general rule, the death of an offeror will terminate the offer where the offeree has notice of the death. Where the offeree does not have notice of the offeror's death, whether the offer terminates will depend upon whether it is still possible for the offeror's obligations to be fulfilled. For example, an offer for the offeror to personally perform services will terminate upon the offeror's death.

3.26 Where an offer is made to a specific offeree, the offeree's death will generally terminate the offer.

How does a Court determine whether there has been acceptance of an offer?

3.27 An acceptance is an unqualified assent to the terms of an offer. As stated above, acceptance on different terms to the offer is not acceptance capable of giving rise to the formation of a contract. Rather, it is construed as a counter-offer that impliedly rejects the offer and requires acceptance before becoming binding.

3.28 In the case of a unilateral contract, it may not always be clear whether a person has done a certain act capable of accepting the offer in response to the offer or for some other reason. While an offeree's conduct is normally assessed by reference to external manifestations, or objective evidence, performance of a requested act will not give rise to a unilateral contract if the evidence establishes that the offeree was not in fact acting in response to the offer.

3.29 For example, in *Crown v Clarke* (1927) 40 CLR 227, a monetary reward was offered for information leading to the conviction of people responsible for murdering police officers. One month after seeing the reward, Clarke was charged in connection with the crime and gave a statement which led to the conviction of others. He claimed the reward.

3.30 The Court held that in providing the information leading to conviction of others, Clarke was acting to secure his own release and not in response to the offer of reward. Although performance of an act (or acts) specified in an offer as constituting acceptance may be presumed to be performed in response to an offer, this presumption was rebutted.

3.31 A contract cannot be forced on the offeree by stipulating silence as the prescribed method of acceptance. However, silence may indicate acceptance in some circumstances. The ultimate issue is whether a reasonable bystander would regard the offeree's conduct, including the offeree's silence, as signalling the acceptance of the offer.

3.32 For example, where an offeree with a reasonable opportunity to reject the offer of goods or services takes the benefit of them under circumstances which indicate that they were to be paid for in accordance with the offer, a reasonable bystander would have concluded that the offer was accepted (*Empirnall Holdings Pty Ltd v Machon Paull Partners Pty Ltd* (1988) NSWLR 523).

3.33 Where the acceptance of an offer is posted in the mail, the postal acceptance rule applies. This rule specifies that where the circumstances are such that the offeror must have intended that the offer could effectively be accepted by the act of posting a letter of acceptance, the acceptance is complete as soon as it is posted (*Henthorn v Fraser* [1892] 2 Ch 27; *Brinkbon Ltd v Stahag Stahl Und Stahlwarenhandelsgeslleschaft mbH* [1983] 2 AC 34).

4. Consideration

4.1 Consideration is the price that is asked by the offeror in exchange for the offer. "Price" is not limited to a monetary price, but can also be the incurring of an obligation. For

example, consideration may be the offer to exchange one service provided by the offeror for another provided by the offeree.

4.2 In legal terms, consideration is a detriment or liability voluntarily incurred or a benefit conferred on the promisor at the instance of the promise in exchange for the promise. It is also referred to as *quid pro quo.*

4.3 Consideration is an essential requirement for an enforceable contract. Without consideration, a promise is unenforceable at law.

4.4 There are a number of general rules that the Courts apply about consideration.

The benefit/detriment requirement

4.5 The first aspect of valuable consideration is that it must consist of a detriment to the promisee or a benefit to the promisor. As stated above, "price" is used in the broad sense to describe consideration and need not be monetary. However there must be some benefit or detriment that passes between the parties.

The bargain requirement

4.6 The modern theory of consideration has arisen from the notion that a contract is a bargain struck between the parties by an exchange. According to that theory, consideration must be satisfied in the form of a price *in return for* the promisor's promise.

4.7 The second requirement is therefore that the benefit conferred on the promisor or the detriment suffered by the promisee must be given in return for the promise. In other words, the act relied on as consideration must be performed as the agreed price of the promise – there must be a relation of quid pro quo.

4.8 The 'bargain' aspect of consideration will be satisfied if the acts which are said to amount to consideration have been performed at the request or implied request of the person making the promise.

Case study: *Australian Woollen Mills Pty Ltd v Commonwealth* (1954) 92 CLR 424

As part of a scheme to encourage the purchase of wool in the aftermath of World War II, the government offered a subsidy for manufacturers purchasing wool for use in local manufacture. The plaintiff purchased wool and used it for this purpose and received some payments. The Government subsequently stopped payments. The plaintiff claimed the subsidy, arguing that there was a contract to pay the subsidy.

The High Court rejected the claim that a contract had formed between the plaintiff and the Commonwealth. The High Court stated that in order for a contract to be established, it was necessary that the statement or announcement relied upon as a promise was really offered for consideration

for the doing of the act, and that the act was really done in consideration of a potential promise inherent in the statement or announcement. There must be a relation of quid pro quo between the statement or announcement and the act that is relied upon as consideration for the alleged promise.

Adequacy of consideration

4.9 The phrase “adequacy of consideration” refers to the intrinsic value of the benefit or detriment. An inquiry into the sufficiency of consideration involves the question whether, for what are ultimately public policy reasons, certain consideration should be denied legal efficacy.

4.10 The general principle is that the courts do not inquire into the adequacy of consideration, that is, the comparative value of the consideration and the promise or act in return for which it is given.

4.11 The most famous case regarding the nature of consideration is *Chappell & Co Ltd v Nestle Co Ltd* [1960] AC 87 in which the Court expressed the view that a 'peppercorn' could constitute valuable consideration (if stipulated by the promisor) even if the promisor was not fond of peppers and would discard the corn.

4.12 In *Woolworths Ltd v Kelly* (1991) 22 NSWLR 189, the Court indicated that courts do not inquire into the adequacy of consideration because:

(a) Courts have no way of assessing the value a particular person places on the consideration they have contracted to receive.

(b) Any requirements of adequacy of consideration would render the enforceability of contracts uncertain.

(c) The Courts’ stance protects economic freedom, even though ‘[t]hat liberty extracts a price in social terms.

(d) Economic efficiency is best pursued through voluntary exchanges; the role of the courts should thus be limited to ensuring that a bargain has been struck and an exchange made.

Sufficiency of consideration

4.13 Although the courts will not inquiry into the adequacy of consideration (i.e. whether the bargain is *worth* what the parties agreed to), the courts do consider the question of whether there has been *sufficient consideration* to give rise to formation of a contract. This issue arises in particular in the following ways.

Past consideration

4.14 Consideration must come into existence either at the same time or after the promise. Where the stipulated consideration pre-dates the promise, it will not be considered sufficient consideration.

4.15 For example, a promise by Sam made on 30 March to pay $200 to Mike for services Mike provided on 1 February will not give rise to a binding contract as the service performed by Mike is past and cannot provide consideration supporting Sam's later promise.

4.16 The courts have recognised an exception to the principle in the case to pay for past services which were rendered on the basis that they were to be paid for.

Promise to perform existing legal duty

4.17 A promise to perform an existing contractual duty is, generally, not regarded as sufficient consideration unless some additional benefit is conferred.

4.18 This often arises in the context of a one-sided modification of an existing contract. However, an exception arises where one party to the contract promises to do something more than what was originally promised, as part of a later agreement.

4.19 A common scenario is where there has been part payment of a debt owing under a contract. For example, if A owes B $100 pursuant to an existing contract, and has already paid $50, does a promise by A to pay B an additional $20 in exchange for waiving the remaining debt of $30 constitute consideration?

4.20 The general rule is that A's promise to pay B $20 in full settlement of the debt will not, on its own, be contractually binding on B. However, there are some exceptions to this rule. For example, where A's promise will provide a distinct factual benefit to B, it will be good consideration.

Case study: *Williams v Roffey Bros and Nicholls (Contractors) Ltd* (1990) 1 All ER 512

The plaintiff was a carpentry sub-contractor who found himself in financial difficulties when he was more than half-way through completing the sub-contract. The sub-contract price turned out to be too low to enable him to complete the work at the agreed price. The sub-contractor therefore told the defendant (the head builder) that unless he agreed to pay him extra, he would have to cease work. The builder agreed to pay the extra amount. The question for the Court was whether he was liable for this amount.

The UK Court of Appeal held that the builder was liable for the additional amount as there was "practical benefit" that accrued to the builder. Specifically:

4.21 The extra payment ensured that the sub-contractor would continue working;

4.22 The builder would not incur the penalty for the delay in its own contract with the owner of the property; and

4.23 The builder would avoid the trouble and expense of having to engage another sub-contractor.

4.24 This UK authority has been applied in Australia: see *Musumeci v Winadell Pty Ltd* (1994) 34 NSWLR 723. In that case, *William v Roffey Bros* was applied by Santow J in a modified form; the "practical benefit" exception was qualified in three ways:

(a) The principle was extended to cover a situation in which the modifying party makes a concession, such as accepting a reduction in the beneficiary's obligations.

(b) In order to protect against coercive modifications, the practical benefit principle should apply only where the promise has not been induced by 'unfair pressure'.

(c) A practical benefit should only constitute good consideration if the beneficiary's performance is capable of being regarded by the modifying party as worth more than any remedy against the beneficiary.

4.25 As such, in order for past consideration to fall within this exception, it must also be established that the promise given by B to accept past consideration was voluntary, and not given as a result of conduct amounting to duress, fraud, undue influence or unconscionable conduct.

Promises made to third parties

4.26 A promise to perform an existing contractual obligation does amount to good consideration if it is made to a person who was not a party to the original contract.

4.27 The existing legal duty rule does not apply because the promisor incurs an additional legal obligation, and confers an additional legal right on the new promisee.

Bona fide compromises

4.28 A promise to perform an existing legal obligation will constitute good consideration where it is made by the beneficiary as part of a bona fide compromise of a disputed claim, the promisor having asserted that he is not bound to perform the obligation under the pre-existing contract or that he has a cause of action under that contract.

4.29 This will arise in the context of litigated or other disputes. For example, if there is a dispute about whether A owes B $100 under an existing contract, and in the course of that dispute, A offers to pay $50 to settle the dispute, B's promise to accept $50 from A is full and final settlement of the dispute constitutes good consideration.

4.30 It is not necessary for the promisor to establish that he or she had a valid legal entitlement to refuse to perform the contract. it is enough that they intimated that they did not consider themselves bound to perform and that their claim was honestly made.

Illusory consideration

4.31 A promise will be *illusory* if the promisor has an unfettered discretion in relation to performance. For example, if a contract specifies that person A may *elect* at their discretion to provide services to person B, A's promise is illusory.

4.32 The effect of an illusory promise can be analysed in two ways:

(a) An illusory promise will not constitute good consideration for a counter-promise made by another party. That is, if one party makes only illusory promises, then the entire contract will fail for want of consideration.

(b) A contract containing an illusory promise may be regarded as incomplete. The entire contract will be regarded as illusory where an essential term has been left to be determined by one of the parties.

4.33 Generally, an illusory promise will have the first consequence: wherever words which by themselves constitute a promise are accompanied by words showing that the promisor is to have a discretion or option as to whether he will carry out that which purports to be the promise, the result is that there is no contract (*Placer Development Ltd v Commonwealth* (1969) 121 CLR 353).

4.34 However, some promises may at first appear illusory, but in fact remain enforceable. For example, a promise that is *contingent* upon an event is not illusory. This means that the obligation to perform the promise will only arise upon the happening of an event.

4.35 A common example of contracts that fall into this category are "subject to finance" contracts. In those contracts, one party's obligation to perform the contract by paying a specified amount only becomes enforceable once they have received finance to enable them to pay from a third party (*Meehan v Jones* (1982) 149 CLR 571).

5. Intention to Create Legal Relations

5.1 As well as evidence of *agreement* and *consideration*, the third key requirement for formation of a contract is an intention to create legal relations. It is this element that distinguishes a contract from informal promises (for example, a promise to your partner to do the washing up if he or she cooks dinner).

5.2 As with other aspects of contract law, whether or not the parties intended to create legal relations, i.e. whether they intended to bound by their promises, will be determined *objectively*, as distinct from any uncommunicated subjective reservation or intention on the part of either party. A court will consider what has objectively been conveyed by what has been said and done, having regard to the circumstances in which those communications and actions happened.

5.3 In *Ermogenous v Greek Orthodox Community of SA Inc* (2002) 209 CLR 95 at 109, the High Court explained that in determining whether the parties intended to create legal relations, it is relevant to consider:

(a) The subject matter of the agreement;

(b) The status of the parties, and their relationship to each other; and

(c) Other surrounding circumstances.

5.4 In the context of intention to create legal relations, reference is made to "presumptions".

5.5 For example, it is said that there are some family arrangements which are not intended to give rise to legal relationships. Where a parent purchases property in the name of their child, the *presumption of advancement* assumes that the purchase of property was intended as a gift, rather than there being an intention to create legal relations in the form of a debt.

5.6 In contrast, the courts adopt a presumption that commercial transactions are intended to create legal intentions. This means that a person seeking to deny the enforceability of a commercial transaction bears the onus of proving that it was not intended to be binding. As such, statements that are promissory in nature in a commercial context will be enforceable unless it is expressly stated that they are not intended to be so (*Banque Brussels Lambert v Australian National Industries Ltd* (1989) 21 NSWLR 502).

5.7 Similarly, an intention to create legal relations is likely to be manifested when a government enters into a commercial transaction expressed in contractual language (*Placer Development Ltd v Commonwealth* (1969) 121 CLR 353). However, where the administrative or political activities of government are concerned, the courts are likely to find that an intention to create legal relations does not exist (*Administration of Papua New Guinea v Leahy* (1961) 105 CLR 6).

5.8 Each of these presumptions are rebuttable. This means that a court will not necessarily apply the presumption if there is evidence to the contrary.

Preliminary agreements or agreements to negotiate

5.9 Parties who have negotiated the principal terms of a proposed transaction may enter into a preliminary written agreement, with the intention of recording their agreement in a more formal way at some time in the future.

5.10 The effect of a preliminary agreement depends upon the intention disclosed by the language used by the parties. The use of expressions such as "*subject to contract*" and "*subject to formal contract*" prima facie indicate that the parties have done no more than establish a basis for a future agreement, and that the preliminary agreement is not intended to be binding.

5.11 However, the fact that a formal contract is intended to include further terms will not prevent the preliminary agreement from being binding, provided those further terms can be settled without agreement between the parties. In contrast, an agreement cannot be binding if it depends on further agreement between the parties.

5.12 The High Court considered this issue in the seminal case of *Masters v Cameron* (1954) 91 CLR 353. The Court stated that a preliminary agreement will be binding if it appears the parties intended it to be binding and described the following three categories of cases:

(a) The parties may intend to be bound immediately, but propose to restate the terms in a form which is fuller or more precise, but not different in effect.

(b) The parties may have agreed on all the terms of their bargain, and do not intend to vary those terms, but 'have made performance of one or more terms conditional upon the execution of a formal document".

(c) The parties may not intend to make a binding agreement at all unless and until they execute a formal contract.

5.13 The legal implications differ in each category. In the first case, the parties are bound whether or not a formal document is ever signed.

5.14 In the second category, the parties are bound to bring the formal document into existence.

5.15 In the third category, the parties are not bound unless a formal document is signed.

6. Contracts Requiring Written Evidence

6.1 The general rule is that contracts can be written or oral, express or implied.

6.2 However certain categories of contract must be in writing. This requirement is governed by statute and differs in the different Australian jurisdiction.

6.3 Some common examples of contracts that must be in writing include:

(a) Contracts for the sale of land: see s 126, *Instruments Act 1958* (Vic); s 54A(1), *Conveyancing Act 1919* (NSW); s 59, *Property Law Act 1974* (Qld); s 26(1), *Law of Property Act 1936* (SA); *Statute of Frauds 1677* (Imp) (WA); s 36, *Conveyancing and Law of Property Act 1884* (Tas); s 201, *Civil Law (Property) Act 2006* (ACT); s 62, *Law of Property Act 2000* (NT).

(b) Bill of exchange and promissory notes: *Bills of Exchange Act 1909* (Cth).

(c) Cheques and payment orders: *Cheques and Payment Orders Act 1986* (Cth).

(d) Assignments of copyright: *Copyright Act 1968* (Cth).

(e) Binding financial agreements: *Family Law Act 1975* (Cth).

CHAPTER 3 – PARTIES TO THE CONTRACT

7. Overview

7.1 This Chapter considers two key concepts in contract law:

(a) A party's *capacity* to enter into a contract; and

(b) Who is bound by the contract, that is, *privity of contract.*

8. Capacity

8.1 Capacity refers to a party's legal ability to enter into a contract. The requirement is intended to assist and protect people who are incapable of entering into a contract or may not understand the consequences by reason of their age or mental capacity.

Age

8.2 The age of majority in Australia is 18. The general rule at common law is that a contract made by a minor is *voidable.* This means that the contract can be undone at the election of the minor. It is not automatically invalid and non-binding.

8.3 There are exceptions to this rule. At common law, a contract by a minor for necessities is binding on both parties: *Nash v Inman* [1908] 2 KB 1.

8.4 In all states other than NSW, the sale of goods legislation provides that where "necessaries" are sold and delivered to a minor, the minor must pay a reasonable price: s 7, *Sale of Goods Act 1954* (ACT); s 7, *Sale of Goods Act 1972* (NT); s 5, *Sale of Goods Act 1896* (Qld); s 2, *Sale of Goods Act 1895* (SA); s 7, *Sale of Goods Act 1896* (TAS); s 7, *Goods Act 1958* (Vic); s 2, *Sale of Goods Act 1895* (WA).

8.5 In NSW, minors are presumed to be bound when they enter into contracts if the contract is for their benefit: *Minors (Property and Contract) Act 1970* (NSW).

Mentally disabled and intoxicated persons

8.6 A contract is voidable at the option of a party who, as a result of mental disability or intoxication, is unable to understand the nature of the contract being made. provided that the other party knew, or ought to have known, of that person's disability or intoxication: *Gibbons v Wright* (1954) 91 CLR 423.

8.7 This means that a contract will not necessarily be invalid if it is made with a person who has a mental disability or was intoxicated at the time. The Court will need to determine the factual matters set out above, namely whether the person was able to understand the nature of the contract being made, and whether the other party was aware of the disability or intoxication.

Corporations

8.8 Section 124 of the *Corporations Act 2001* (Cth) provides that a company has the legal capacity and powers of an individual as well as all of the powers of a body corporate. Accordingly, a corporation at law has the capacity to enter into a contract.

8.9 A company's power to make, vary, ratify or discharge a contract may be exercised by an individual acting with the company's express or implied authority, and on behalf of the company: s 126, *Corporations Act.*

8.10 A company may execute a contract either by use of the company's common seal or, alternatively, without the common seal if the contract is signed by two directors, or a director and a company secretary, or, for a proprietary company that has a sole director who is also the sole company secretary, that director: s 127, *Corporations Act.*

9. Privity of Contract

9.1 *Privity of contract* refers to the rule that that only a person who is a party to a contract can enforce the contract and incur obligations under it.

9.2 Therefore, if A enters into a contract with B, A's associate, C, does not have privity of contract and cannot enforce A's rights under the contract.

9.3 Further, in this same example, the contract between A and B cannot impose obligations on C.

9.4 A common example occurs in construction contracts. If A contracts with B for B to build A's house, and B sub-contracts to C, a carpenter, A cannot require C to provide carpentry services to A.

CHAPTER 4 – THE TERMS OF THE CONTRACT

10. Overview

10.1 This Chapter considers the following topics:

(a) What terms are included in a contract;

(b) What happens if the contract is incorrectly recorded?;

(c) Interpretation of contractual terms by reference to oral evidence; and

(d) Variation of contracts.

11. Terms of the Contract

11.1 The *terms of the contract* mean the content of the contract. What have the parties each promised to do according to the terms of the contract? This might be something as simple as paying the price of goods that will be purchased, or it could be complicated terms regarding contract obligations in a construction contract.

11.2 Contractual terms can be express or implied. Express terms are those that are expressly stated to be part of the contract. Implied terms are not expressly stated.

11.3 The courts are slow to imply a term into a contract. In many cases, what the parties have actually agreed upon represents the totality of their willingness to agree. That is, each party may have been prepared to take his or her chance in relation to an eventuality for which no provision is made in the contract. The more detailed and comprehensive the contract the less ground there is for supposing that the parties have failed to address their minds to the question at issue.

11.4 The three main reasons for implying terms into a contract are as follows.

(a) The need to give business efficacy to a contract;

(b) Terms implied from the nature of the contract itself;

(c) Terms implied because of custom or trade usage. For this category, there must be evidence that the custom relied on is so well known and acquiesced in that everyone making a contract in that situation can reasonably be presumed to have imported that term into the contract; and

(d) Terms may be implied by reason of legislative requirements.

11.5 The first three categories are *contract terms implied in fact.* The last category comprises *contract terms implied by law.*

Contract terms implied in fact: Requirements

11.6 The following conditions must be met before a term can be implied into a contract in fact (*Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337):

(a) It must be reasonable and equitable;

(b) It must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it;

(c) It must be so obvious that 'it goes without saying';

(d) It must be capable of clear expression; and

(e) It must not contradict the express terms of the contract.

Contract terms implied by law

11.7 The key category of contracts containing terms implied by law are *contracts for the sale of goods.* Those contracts contain the following implied terms:

(a) An implied term that the seller has a right to sell the goods at the time when the property is to pass to the purchaser;

(b) An implied warranty that the buyer shall have and enjoy quiet possession of the goods; and

(c) An implied warranty that the goods shall be free from any charge or encumbrance in favour of any third party not declared or known to the buyer before or at the time when the contract is made.

11.8 Previously, consumer law implied terms into consumer law. The Australian Consumer Law (ACL) now applies nationally to consumer contracts. Rather than imply terms into a contract, the ACL contains a number of statutory guarantees, including a guarantee that goods and services are fit for purpose. Because these take the form of a guarantee rather than an implied contractual term, the remedy are found in the ACL rather than through a breach of contract claim, although the consequence is in effect the same.

12. Rectification

12.1 Where a term which was actually agreed upon by the parties was omitted from a contract, the courts will rectify the contract by including the term which should have been included. The courts will imply that the term is one which it is presumed that the parties would have agreed upon had they turned their minds to it, although it is not a term that they have actually agreed upon. In other words, a court may rectify a contract where the parties simply wrote the terms down incorrectly.

12.2 A party seeking rectification of a contract must prove three elements:

(a) Intention: it must be shown that the parties had a common intention which continued until the time when the document was executed. The time at which the parties held the intention is crucial. If the plaintiff proves the parties intended something at one time, but the defendant proves that they changed their intention prior to signing the document, rectification will not be granted (see, for example, *Maralinga Pty Ltd v Major Enterprises Pty Ltd* (1973) 128 CLR 336).

(b) The parties intended that the written instrument was to conform to this common intention.

(c) The written instrument does not in fact reflect this common intention because of a common mistake

13. Interpretation of the Contractual Terms: The Parol Evidence Rule

13.1 When contractual disputes reach court, it is often because there is a dispute about how a contract can be interpreted. Although the contract may be in writing, sometimes, particularly in complex contracts, it will not be clear what the parties intended by particular words and terms in the written contract.

13.2 As a general rule, where the terms of a contract are recorded in writing, extrinsic evidence, including oral (or "parol") evidence is not admissible to show that there are other terms included in the contract other than those that have been noted in the written contract or in interpreting the terms that are included in the written contract. This means, for example, that evidence of parties' conversations or communications prior to the formation of the contract cannot be used to interpret the terms of the contract. Similarly, evidence of negotiations or post-contractual communications are not admissible to interpret the written contract.

13.3 Because the parol evidence rule applies to written contracts, it does not apply to contracts that are partly in writing and partly oral, or wholly oral contracts.

13.4 There are several exceptions to the parol evidence rule. These include:

(a) Where a contract is *ambiguous*, the court will look at the *factual matrix* (that is, the surrounding facts and circumstances) to assist in discerning the intended meaning of the contract.

(b) Where evidence of pre-contractual statements or negotiations are said to constitute terms of the contract, the evidence is admissible to determine whether those terms have been integrated into a contract.

(c) Evidence related to the enforceability of the contract, including evidence of mistake or misrepresentation, is admissible.

14. Variation of Contract

14.1 The terms of a contract may be varied by the consent of the parties. However, it is important to remember that the general rules relating to formation of a contract also apply to variation.

14.2 Most significantly, consideration must pass for a variation of a contract to be effective. As discussed above, a variation of a contract for past consideration will not be effective.

14.3 This means that where, for example, A has agreed to pay B for B's services, and the parties agree to vary the contract by a reduction in the price that A will pay B, the variation will not be legally effective if B continues to agree to perform the same services. There must be some corresponding amendment in B's rights or obligations, subject to the exceptions discussed above.

14.4 One way in which parties frequently seek to avoid this requirement is by negotiating variations to contract by *deed.* A deed may have a similar appearance to a contract but has one significant difference: a deed does *not* require consideration whereas a contract does.

14.5 A deed is considered binding due to its form. As such, there are strict requirements for a valid deed. Specifically, a deed must be:

(a) In writing on paper;

(b) Signed with an intent to execute the instrument as a deed;

(c) Sealed; and

(d) Delivered.

CHAPTER 4 – VITIATING FACTORS

15. Overview

15.1 This Chapter considers the circumstances in which a contract will be varied by the courts or undone because of factors that occurred at the time when the contract was entered into.

15.2 Specifically, this Chapter examines the effect of the following:

(a) Misleading or deceptive conduct;

(b) Mistake;

(c) Duress;

(d) Undue influence;

(e) Unconscionable conduct; and

(f) Unfair contract terms.

16. Misleading or Deceptive Conduct

16.1 Section 18 of the ACL provides that a person must not, in trade or commerce, engage in conduct that is misleading or deceptive or that is likely to mislead or deceive.

16.2 The prohibition on misleading or deceptive conduct is primarily intended to protect consumers, however it is not limited to consumer transactions. The protection offered by s 18 extends to statements made in the negotiation of individual contracts made in trade or commerce.

16.3 The phrase “trade or commerce” has been interpreted broadly, but excludes purely private sales such as the sale of residential property between homeowners.

16.4 A similar prohibition is contained in the *Australian Securities and Investments Commission Act 2001* (Cth) (ASIC Act). Section 12DA prohibits misleading or deceptive conduct in relation to financial services. This covers contracts in relation to financial products, including credit contracts and financial services.

16.5 In considering whether conduct is misleading or deceptive, a court will consider the conduct in question in light of the relevant surrounding circumstances. The following principles apply (*ACCC v Dukemaster* [2009] FCA 682):

(a) The conduct must lead, or be capable of leading, a person to error.

(b) Conduct is likely to mislead or deceive if there is a real or not remote chance or possibility, regardless of whether it is less or more than 50 percent.

(c) The test is objective: the Court must determine for itself whether the conduct was misleading or deceptive.

(d) Contravention of s 18 does not depend on showing intention on the part of the party making the representation or its belief concerning the accuracy of the statement of fact but whether the statement conveys a meaning which is false.

(e) A statement of opinion will not be misleading or deceptive or likely to mislead or deceive merely because it turns out to be incorrect, misinforms or is likely to do so.

(f) However, an opinion may convey that there is a basis for it, that it is honestly held and when it is expressed as the opinion of an expert, that it is honestly held upon rational grounds involving an application of the relevant expertise.

16.6 Generally, misleading or deceptive conduct requires positive conduct on the part of the representor. However, in certain limited circumstances, silence can amount to misleading or deceptive conduct.

16.7 Mere silence, without more, is unlikely to constitute misleading or deceptive conduct. However, remaining silent will be misleading or deceptive if the circumstances are such as to give rise to a reasonable expectation that if some relevant fact does exist, it will be disclosed (*Australian Securities and Investments Commission v ActiveSuper Pty Ltd (in liq)* [2015] FCA 342).

16.8 Examples of claims under s 18 of the ACL involving contractual disputes include the following:

(a) *Tsang v Uvanna Pty Ltd* (1996) 140 ALR 273: 18 applicants of Chinese origin succeeded in claims of misleading and deceptive conduct against an immigration agent who charged large fees to secure permanent residency in Australia for applicants.

(b) *Larsson v Dudney* [2018] QCA 250: the appellant succeeded in establishing that the respondent engaged in misleading and deceptive conduct when he sold a catamaran to the appellant for charter work without revealing that the vessel had a history of engine failures.

(c) *Commonwealth Bank of Australia v Groves* [2012] SASC 110: in response to a claim by the bank for repayment of a substantial sum, the defendant counter-claimed for damages based on allegedly misleading conduct by the bank when the loan was taken out.

(d) *TSG Franchise Management Pty Ltd v Cigarette & Gift Warehouse (Franchising) Pty Ltd (No 2)* [2016] FCA 674: the respondent was found to have engaged in misleading and deceptive conduct in the assertions it made to members of a rival franchise group in encouraging them to cancel their current franchise and become a franchisee of the respondent.

(e) *Taylor v Gosling* [2010] VSC 75: a retired couple who were novice investors invested in a syndicate to develop an apartment complex after attending an investment seminar. They succeeded in establishing that the salesperson who

spoke at the seminar and later convinced them to put up further funds had engaged in misleading and deceptive conduct.

16.9 Once it has been established that a pre-contractual misrepresentation constitutes misleading or deceptive conduct, the ACL provides a number of different remedies that are available.

Damages

16.10 A person who suffers loss or damage by reason of conduct which is misleading or deceptive may be awarded damages.

16.11 Damages are discussed in further detail below. In summary, damages are intended to compensate a person for the loss caused by the misleading or deceptive conduct.

16.12 For example, if a seller misrepresents the nature of goods that they are providing and induces a person to purchase the goods based upon the representation, the purchaser may be entitled to damages for their loss, usually the amount that they have paid for the goods.

Other orders

16.13 The ACL grants the Court wide discretion as to the appropriate remedy when misleading or deceptive conduct has been established. These remedies include the following:

(a) An order declaring the contract to be wholly or partially void;

(b) An order varying the contract;

(c) An order refusing to enforce any or all of the provisions of the contract;

(d) An order directing a refund of money; and

(e) An order for the repair of goods or directing the supply of parts.

17. Mistake

17.1 The situation where both parties to a contract make a mistake in the written form of the contract is addressed above in the “Rectification” section. However, what is the situation if only one party is mistaken as to the terms of the contract? Does the contract remain enforceable, or is the mistaken party afforded an opportunity to avoid the operation of the contract? Other categories of mistake may also arise that have legal consequences on the validity of a contract.

17.2 The common law gives very few remedies where a unilateral mistake has occurred in entering into the contract. This is because if a subjective mistake is treated as having a consequence at common law, the contract would be void from the outset of its

operations. This can have drastic consequences if one party has already commenced performing the contract or has relied upon its validity in some other way.

17.3 In contrast, equity takes a more flexible approach. Equity treats mistakes as rendering the contract as *voidable* rather than void. That is, the binding nature of the contract *may* be avoided, but will not automatically be deemed invalid from the outset. A voidable contract is one which may be set aside (rescinded) and the parties restored to the position they were in before the contract was made. A contract may be rescinded *on terms* which aim and achieving fairness between the parties.

17.4 As discussed above, the remedy of rectification may also be available.

17.5 Cases involving mistake fall into two broad categories:

(a) Cases where the parties are in agreement, but they both erroneously assume some fundamental matter to be true; or

(b) Cases where the parties are so much at cross-purposes that it can be said that they are not in actual, subjective agreement.

Parties in agreement

17.6 This category of mistake arises where the parties have reached consensus, but they both make the same false assumption in respect of a fundamental matter, such as the very existence of the subject matter or an important quality of the subject matter, or in recording their common intentions.

<u>Mistake as to the existence of subject matter</u>

17.7 Where the parties are mutually mistaken about the existence of subject matter, there are three potential ways of analysing the situation (*McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377):

(a) Implied condition precedent: this means that implied in the contract is a condition which must be fulfilled before the parties' obligations under the contract arise. If the parties are mistaken as to the subject matter of the contract and the term is implied, the parties' obligations to fulfil the contract never arises at law.

(b) Implied promise: according to this analysis, the contract exists with an implied promise as to the subject matter. Therefore, for example, if A contracts with B to sell B a house with a garage, and in fact there is no garage on the property, the law would treat A as having impliedly promised that there was a garage on the property.

(c) Mistake: in the case of mistake, the contract is effectively treated as if it did not come into existence. However, a party cannot rely on a mistake induced by their own negligence.

Case study: *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377

McRae won a tender from the Commonwealth Disposals Commission to retrieve an oil tanker from a reef. However, when McRae went to retrieve the tanker, he discovered that the tanker did not exist.

The Commission argued that it was not liable for damages for breach of contract, as the contract was void by reason of a common mistake that the oil tanker did not exist.

The High Court rejected this argument. The Commission had not made proper inquiries as to the existence of the tanker. The buyers relied upon, and acted upon, the assertion of the seller that there was a tanker in existence.

The Court held that this was not a case in which the parties could be seen to have proceeded on the basis of a common assumption of fact so as to justify the conclusion that the correctness of the assumption was intended by both parties to be a condition precedent to the creation of contractual obligations. The officers of the Commission made an assumption, but the plaintiffs did not make an assumption in the same sense. They knew nothing except what the Commission had told them.

The only proper construction of the contract is that it included a promise by the Commission that there was a tanker in the position specified. The Commission contracted that there was a tanker there.

Mistake as to quality of subject matter

17.8 At common law, in the case of mistake as to quality of subject matter, a mistake will not affect assent unless it is the mistake of both parties. Further, the mistake must be as to the existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be.

17.9 For example, in *Bell v Lever Brothers Ltd* [1932] AC 161, Lever Brothers Ltd had terminated Mr Bell's employment and given him a compensation payment. The company later discovered that Mr Bell had been in breach of the terms of his employment contract, thus entitling the company to terminate the employment without compensation. The company sought to void the agreement to pay compensation on the basis of their mistake. The court rejected this argument and held that the contract was not void, as the mistake was not an 'essential and integral' part of the contract.

Parties not in agreement

17.10 This category of mistake concerns the situation where the parties are so much at cross-purposes that it can be said that there is no consensus or actual agreement.

17.11 The mistake may relate to the terms of the contract, the identity of the parties, or one party may sign a document believing it has a fundamentally different character from what in fact it has.

Mistake as to terms

17.12 A party who has entered into a written contract under a serious mistake about its contents in relation to a fundamental term will be entitled in equity to an order rescinding the contract if (*Taylor v Johnson* (1983) 151 CLR 422):

(a) The other party is aware that circumstances exist which indicate that the first party is entering the contract under some serious mistake or misapprehension about either the content or subject matter or that term, and

(b) The other party deliberately sets out to ensure that the first party does not become aware of the existence of his mistake or misapprehension.

17.13 In such a situation, the High Court has held that it is unfair that the mistaken party should be held to the written contract by the other party whose lack of precise knowledge of the first party's actual mistake proceeds from wilful ignorance because he or she engages deliberately in a course of conduct which is designed to inhibit discovery of it.

Mistake as to identity

17.14 Where two parties have come to a contract, the fact that one party is mistaken as to the identity of the other does not mean that there is no contract, or that the contract is a nullity.

17.15 Rather it means that the contract is voidable (liable to be set aside at the instance of the mistaken person), so long as the mistaken party applies to set aside the contract before third parties have in good faith acquired rights under it.

Mistakenly signed documents: *non est factum*

17.16 The defence of *non est factum* (not my deed) was originally used where a plaintiff claimed that his or her signature or seal on a deed had been forged.

17.17 *Non est factum* has now been extended to cases where a party seeks to be released from a contract he or she has signed. The rule is that if a person proves that he or she signed a document without carelessness and believing it to be a document fundamentally different from what it was, he or she is not bound by the signature. The defence is not frequently invoked and difficult to establish.

18. Duress

18.1 If a person has entered into a contract by reason of duress, the contract may be liable to be set aside or rescinded.

18.2 The absence of choice in entering into a contract can be proved in various ways, for example by protest, by the absence of independent advice, or by a declaration of intention to go to law to recover the money paid or the property transferred. However none of these matters go to the essence of duress. There are two elements in the wrong of duress (*Universe Tankships of Monrovia v International Transport Workers Federation* [1983] 1 AC 366):

(a) Pressure amounting to compulsion of the will of the contracting party; and

(b) Illegitimacy of the pressure exerted.

18.3 Traditionally at common law, a wrongful coercive method of procuring a contract was called duress and was narrow in scope: it was concerned with promises procured by actual or threatened violence to the person, or unlawful imprisonment.

18.4 However this traditional conception of duress has been extended in more recent times. Economic duress has now been recognised by the Courts to be a form of duress which may vitiate agreement to a contract. Interference with contractual rights has been recognised as a possible form of illegitimate pressure, even though the promise extracted is supported by consideration.

18.5 Relief will not be granted, however only on the basis of an inequality, even a great inequality, of bargaining position. Relief may, however, be appropriate when the disparity was substantially brought about by the other party's prior conduct. The exploitation of the inequality could then be described as 'unconscientious.

Case study: *Universe Tankships of Monrovia v International Transport Workers Federation* [1983] 1 AC 366

A ship belonging to the appellants had been "blacked" by the defendant union, meaning that the union had refused to service the ship at port. Negotiations to clear the threat resulted in payment by the appellants to a welfare fund of the defendant. The company sought its refund saying that it had been paid under duress.

The House of Lord recognised that the payment had been made by duress. The pressure that had been applied by the union was illegitimate. The company's will had been coerced in a way that vitiated its consent. Accordingly, the company could recover its money.

18.6 Section 50 of the ACL now also provides remedies for duress. Section 50 provides that a person must not use "physical force or undue coercion or harassment" in connection with:

(a) The supply or possible supply of goods or services; or

(b) The payment for goods or services; or

(c) The sale or grant, or possible sale or grant, of an interest in land; or

(d) The payment for an interest in land.

19. Undue Influence

19.1 Undue influence occurs where one party to a contract takes advantage of its relationship or position of power over the other party to the contract. This inequality between the parties can result in one party's consent being vitiated and the contract being invalid.

19.2 Undue influence falls into two categories of cases:

(a) Deemed: in this category, the relationship between parties is such that there is a presumption of undue influence. Examples of such relationships include parent/child, guardian/ward, religious advisor/disciple, solicitor/client, and doctor/patient.

(b) Actual: this category is not concerned about general category of relationship, but rather considers whether there was actual influence exercised in the formation of the contract.

19.3 The first step is to consider the relationship between the parties. If there is a prior relationship of confidence such as the categories set out above, the onus of proof will lie on the party seeking to enforce the contract to show that the individual's will was not overborne.

19.4 If, however, there was no such category, the onus lies on the party seeking to set aside the contract to show that there was actual undue influence.

19.5 The most straightforward way for a party to show that there was *not* undue influence is to point to the provision of independent legal advice. There is no rule of law, however, that in order to rebut the presumption, the weak party must be shown to have received such advice, particularly if the court is of the opinion that the independent advice would not have had any effect on the transaction (Union Fidelity Trustee Co of Australia Ltd v Gibson [1971] VR 573).

19.6 *Westmelton (Vic) Pty Ltd v Archer and Schulam* [1982] VR 305, for example, was a case of *presumed* undue influence by reason of the relationship between the contracting parties: that of solicitor and client. The client had not received any independent legal advice prior to entering into the transaction.

19.7 Nonetheless, the presumption of undue influence was rebutted. This was because of the following factors:

(a) The client (a company) had better knowledge of the value of the transaction than the solicitor;

(b) The solicitor was asked to leave the meeting of the company when the actual decision was made;

(c) The solicitor did not initiate the contract; and

(d) There was adequate consideration. Although the Courts will not ordinarily inquire into the adequacy of consideration, the fact that consideration was inadequate may suggest that there was undue influence exercised in the making of the contract.

19.8 The true test is whether the person in whom the confidence is reposed has rebutted prima facie presumption by showing that the 'weaker' party acted of his or her own free will and was not materially affected by confidence reposed on confidant.

20. Unconscionable Conduct

20.1 Like undue influence, unconscionable conduct deals with the relationship between the parties to the contract in circumstances where one party is in a weaker position or position of disadvantage compare to the other contracting party. However while undue influence, like duress, looks at the quality of consent or assent of the weaker party, unconscionable dealing looks at the conduct of the stronger party in attempting to enforce, or retain the benefit of, a dealing with a person under a special disability in circumstances where it is not consistent with equity or good conscience that he or she should do so.

20.2 The focus of the law of unconscionable conduct is therefore on the person in the position of advantage. A court will consider whether it is unconscionable that they be allowed to retain the benefit of the contract.

20.3 There are two elements of unconscionable conduct.

20.4 *First*, is there a relevant *disability* that leads to an inequality between the parties. The term disability does not refer to a physical or mental disability in the ordinary use of the word, but a characteristic of the contracting party, such as age, illiteracy, lack of education or lack of English skills, that render them incapable of properly understanding the legal effect of the contract.

20.5 *Second*, the disability must be sufficiently visible to the other party that it would be unconscionable to enforce the contract.

20.6 In *Blomley v Ryan* (1956) 99 CLR 362, the High Court gave the following examples of disabilities that might lead to the Court finding unconscionable conduct:

(a) Poverty;

(b) Sickness;

(c) Age;

(d) Infirmity of mind;

(e) Drunkenness (although mere drunkenness is insufficient; this characteristic would ordinarily only result in unconscionable conduct if one party has encouraged the other to drink);

(f) Illiteracy or lack of education; and

(g) Lack of assistance or explanation.

20.7 Common to each of these is the fact that the characteristic has the effect of placing one party at a serious disadvantage as compared to the other party.

Case study: *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447

Two elderly migrants who were unfamiliar with written English were asked by their son to mortgage their property in order to secure an overdraft of a company controlled by their son. The son had told his parents that the mortgage was to be limited to $50,000 and to be for six months. This was incorrect.

The bank manager went to the home of the parents and obtained their signature on the guarantee documents. There was very little discussion before the documents were signed. The parents did not read the documents and the bank manager did not explain them.

The High Court determined that the guarantee should be unconditionally set aside on the grounds of unconscionable conduct.

The Court held that the parents were under a special disability when they executed the deed containing the guarantee. The combination of their age, their limited grasp of written English, the circumstances in which the bank presented the document to them for their signature and, most importantly, their lack of knowledge and understanding of the contents of the document meant that they required assistance and advice for there to be a reasonable degree of equality between themselves and the bank.

The disability was sufficiently evident to the bank to make it prima facie unfair or unconscientious for it to be allowed to rely on the guarantee. The onus lay on the bank to show that the guarantee should not be set aside, and that onus had not been satisfied.

Mason J set out the following, oft-cited test in respect of unconscionable conduct. Conduct will be actionable on the grounds of unconscionability in two circumstances:

(a) *first*, when "unconscientious advantage is taken of an innocent party whose will is overborne so that it is not independent and voluntary; and

(b) *second*, when unconscientious "advantage is taken of an innocent party who, though not deprived of an independent and voluntary will, is unable to make a worthwhile judgment as to what is in his best interest".

Case study: *Kakavas v Crown Melbourne Ltd*
(2013) 250 CLR 392

The appellant was a high-stakes gambler and regular patron of Crown's casino. Between June 2005 and August 2006, he turned over $1.479 billion playing baccarat at the casino. He brought a claim
to recover his net loss of $20.5 million over that period.

The appellant claimed that the Casino had engaged in unconscionable conduct by exploiting his gambling addiction and by unconscientiously allowing him and encouraging him to gamble at the Casino. He alleged that the Casino had lured him to gamble at the Casino by providing incentives, such as rebates on losses and use of the casino's private jet.

The High Court rejected the appellant's claim. The Court held that the gambler's pathological interest in gambling was not a special disadvantage which made him susceptible to exploitation by the casino. He was able to make his own rational decisions in his own interests, including deciding at times to refrain from gambling altogether. The Casino did not knowingly victimise the gambler by allowing him to gamble at the Casino.

The Court also held that equity will not intervene to relieve a plaintiff from the consequences of improvident transactions. To deprive a party of the benefit of its bargain on the basis that it was procured by unfair exploitation of the weakness of the other party requires proof of a predatory state of mind.

The principle is not engaged by mere inadvertence, or even indifference, to the circumstances of the other party to an arm's length commercial transaction. Victimisation or exploitation is necessary to engage the principle.

20.8 In addition to equitable remedies, s 20 of the ACL prohibits unconscionability engaged in by a corporation "within the meaning of the unwritten law" (meaning the equitable doctrine of unconscionable conduct). Section 20 thus incorporates into the ACL the equitable principles in relation to unconscionable conduct.

20.9 Further, s 21 provides that a person must not, in trade or commerce, in connection with (a) the supply or possible supply of goods or services to a person, or (b) the acquisition of possible acquisition of goods or services from a person, engage in conduct that is, in all of the circumstances, unconscionable. Section 21 specifically provides that the section is not limited to the unwritten law relating to unconscionable conduct. The section also is capable of applying to a system or conduct or pattern of behaviour.

20.10 Section 12CB of the ASIC Act similarly provides that a person must not, in trade or commerce, in connection with the supply or possible supply of financial services to a person or the acquisition or possible acquisition of financial services from a person, engage in conduct that is, in all the circumstances, unconscionable.

20.11 These provisions mean that most cases involving unconscionable conduct are now brought under the ACL or ASIC Act, rather than in equity. However, this will not always

be the case, for example if the conduct is not in relation to financial services or "in trade or commerce".

21. Unfair Contract Terms

21.1 Section 23 of the ACL provides that a term of a consumer contract is void if the term is unfair and the contract is a standard form contract.

21.2 A *consumer contract* is a contract for the supply of goods or services or for a sale of land to an individual whose acquisition of the goods, services or land is wholly or predominantly for personal, domestic or household use or consumption: s 23(3).

21.3 Section 27(1) creates a rebuttable presumption that a contract is a standard form contract unless proved otherwise. In determining whether a contract is a standard form contract, the Court is required to take into account the factors referred to in s 27(2) being:

(a) whether one party had all or most of the bargaining power relating to the transaction;

(b) whether the contract was prepared by one party before any discussion relating to the transaction occurred with the other party;

(c) whether another party was, in effect, required to accept or reject the terms of the contract, other than the term concerning the subject matter or price of the contract, in the form in which they were presented;

(d) whether the other party was given an effective opportunity to negotiate the terms of the contract other than the term concerning the price of the contract; and

(e) whether the terms of the contract have taken into account the particular characteristics of the party or of the particular transaction.

21.4 Section 24(1) of the ACL provides that a term of a consumer contract is unfair if:

(a) it would cause a significant imbalance in the parties' rights and obligations arising under the contract (s 24(1)(a));

(b) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term (s 24(1)(b)); and

(c) it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on (s 24(1)(c)).

21.5 Section 24(2) of the ACL provides that in determining whether a term of a contract is unfair, the Court must take into account the extent to which the term is transparent and the contract as a whole.

21.6 These provisions of the ACL therefore expand the general law by enabling a Court to invalidate unfair contractual terms. The underlying policy of these provisions is to

respect freedom of contract while seeking to prevent the abuse of standard form consumer contracts which, by definition, have not been individually negotiated (*ACCC v CLA Trading Pty Ltd* [2016] FCA 377).

CHAPTER 5 – TERMINATION OF CONTRACT

22. Overview

22.1 This Chapter considers the circumstances in which contracts come to an end, that is, *termination* of contract.

22.2 In particular, this Chapter examines:

(a) Termination for breach of contract and repudiation; and

(b) Termination by frustration.

23. Termination for Breach and Repudiation

23.1 The most common way that a contract is terminated is by *performance* of the contract. For example, in a contract for a supply of goods, the contract will terminate where one party has supplied the goods and the other party has paid the contracted price.

23.2 Alternatively, the parties may mutually agree to terminate the contract. For example, in the context of an employment agreement, an employee may be offered a new job, and the employee and employer agree to bring the employment contract to an end.

23.3 However, contracts may also be terminated in other, less amicable circumstances. In particular, a party may terminate a contract following the other party's breach of contract or repudiation.

Termination for Breach of Contract

23.4 Where one party to a contract has failed to perform his or her side of the bargain, the party is in *breach of contract*.

23.5 It is important to bear in mind that breach of contract does not automatically terminate the contract. Nor will the party who is not in default necessarily have a right to terminate the contract because of the breach.

23.6 The nature of the promise broken is one of the most important matters in determining whether a right to terminate arises. Simple breaches of contract (for example paying one day late or delivering a product to the wrong address) will not give rise to a right to terminate.

23.7 A right to terminate a contract because of the other party's breach will arise in two circumstances:

(a) a breach of an essential term; or

(b) a sufficiently serious breach of a non-essential term.

23.8 Other breaches of contract will give a party a right to sue for damages arising as a result of the breach, but will not afford a right to terminate the contract.

Breach of an essential term

23.9 Whether or not a term is an essential term is determined by reference to the objective intention of the parties at the time that the contract was entered into. That is, did the parties, viewed objectively, intend for a particular term to be essential to the performance of the contract.

23.10 The parties to a contract may stipulate that a term is an essential term, in which case a Court will respect that. Alternatively, the Court may come to the view that a term is an essential term having had regard to the operation of the relevant term in the context of the contract as a whole.

23.11 In *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd* (1938) 38 SR (NSW) 632, Jordan CJ explained the test as follows:

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

Case study: *Shevill v Builders Licensing Board*
(1982) 149 CLR 620

A lease provided that if rent was unpaid for 14 days or if the tenant was in breach of any of the terms of the lease or if certain other events occurred such as bankruptcy, the landlord might re-take possession of the land.

The tenant was constantly late in paying rent. The landlord re-entered the land and claimed damages for breach of contract for an amount equal to the rent payable over the balance of the term.

The High Court found that the tenant's failure to pay rent did not go to the root of the contract or make further commercial performance of it impossible. In other words, the tenant's actions in paying rent late were not breaches of essential terms of the lease. Accordingly, the landlord was not entitled to terminate the lease.

Breach of a non-essential term

23.12 Breaches of non-essential terms, if sufficiently serious, may also give rise to a right to terminate the contract at common law. Although as a matter of construction of a contract, it may not be the case that *any* breach of a given term will entitle the other party to terminate, some breaches that are serious in nature will give rise to such a right.

23.13 Whether the breach of a non-essential term gives rise to a right to terminate will depend upon the nature of the contract, the nature of the breach, and the consequences for the innocent party.

Termination for Repudiation

23.14 Breach of contract may also arise where there has been an *anticipatory breach.* An anticipatory breach arises where, before the obligation to perform arises, one party terminates the contract in anticipation of the other party's repudiation of the contract or inability to perform.

23.15 *Repudiation* of a contract occurs where one party evinces an intention no longer to be bound by the contract or to perform the contract in a way substantially inconsistent with the party's obligations. That is, the party indicates that he or she does not intend to perform his or her obligations arising under the contract, or not properly perform those obligations, nor enforce his or her rights.

23.16 For example, if a builder announces his or her intention to only construct half of a development, and not the entirety as required by the construction contract, this may amount to a repudiation of the contract.

23.17 Repudiation of a contract will give rise to a right to terminate the contract. Where one party either repudiates the contract or indicates that he or she, although willing to perform, is no longer able to do so, the party will be in breach, and the other party will have a right to *rescind* or terminate the contract.

Case study: *Carr v J A Berriman*
(1953) 89 CLR 327

A building contract required Carr, as the principal, to excavate the site and provide possession of the excavated site to Berriman, the contractor, by a particular handover date. The contract also required the principal to supply certain structural steel to the contractor.

Carr had not even started excavation two months after the handover date and Berriman was informed that the steel was no longer to be supplied by Carr and was to be omitted from the contract.

Berriman refused to proceed with the contract.

The High Court considered that the continuing failure to provide the required possession could demonstrate an intention to no longer be bound by the contract and, therefore, amount to a repudiation of the contract by Carr. The failure to supply the required steel as required by the contract was further demonstration of that intent.

24. Termination by Frustration

24.1 The performance of a contract may sometimes be disrupted by catastrophic events which have not been provided for by the parties in their contract. The doctrine of frustration provides an excuse for non-performance.

24.2 Frustration occurs whenever the law recognizes that without default of either party, a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. In other words, the party would say “This was not what I promised to do." (*Davis Contractors Ltd v Fareham UDC* [1956] AC 696)

24.3 Examples of frustration include the following.

Impossibility of performance

24.4 A party is freed from a contractual obligation when the subject matter of the contract has been destroyed, neither by the act or negligence of the party, unless the party has agreed that he or she will take on the risk of the particular misfortune which has occurred.

24.5 For example, in *Taylor v Caldwell* (1863) 3 B & S 826, the plaintiff had agreed to hire a music hall from the defendant. However before the performance, the music hall was destroyed by fire. The plaintiff sued for breach of contract. The Court released the defendants from their obligations as the contract had been frustrated by the fire.

Frustration of purpose

24.6 Similarly to above, where an event which renders the contract incapable of performance is the cessation or non-existence of an express condition or state of things going to the root of the contract and essential to its performance, the contract is frustrated.

24.7 The seminal case is *Krell v Henry* [1903] 2 KB 740. The defendant had agreed to hire an apartment from the plaintiff on the day of the king’s coronation to watch the coronation parade. The contract did not contain any express terms on the coronation processions or any other purposes for which the flat was to be hired. The processions, however, did not take place on the announced dates. As a result, the defendant declined to pay the balance of the agreed rent.

24.8 The Court held that as both parties recognised that they regarded the taking place of the coronation processions on the days originally fixed as the foundation of the contract, the purpose of the contract was to enable the defendant to watch the procession. The contract had therefore been frustrated and the plaintiff was not entitled to recover the balance of the rent.

24.9 The Court will consider the following in determining whether the purpose of the contract has been frustrated:

(a) having regard to all the circumstances, what was the foundation of the contract?

(b) was the performance of the contract prevented?

(c) was the event which prevented the performance of the contract of such a character that it cannot reasonably be said to have been in the contemplation of the parties at the date of the contract?

Illegality

24.10 If something was illegal at the time the contract was entered into, the *formation* of the contract may be affected.

24.11 In contrast, if some aspect of the performance of a contract becomes illegal *after* the contract is entered into, the contracted may be frustrated.

Limits on the doctrine of frustration

24.12 There are certain limits on the doctrine of frustration that must be borne in mind.

24.13 *First*, the risk of the frustrating event must not have been provided for within the contract. If it was so, it falls within the contemplation of the parties and the parties have allocated risk accordingly.

24.14 *Second*, the purported frustrating event must not be one which the parties could reasonable be thought to have foreseen. That is, if the parties *could* have turned their mind to the risk but did not, the doctrine of frustration will not step in.

24.15 *Third*, the frustrating event must have occurred without fault by the party seeking to rely on frustration.

Effect of frustration

24.16 At common law, where frustration is established, the contract is terminated automatically. There is no option to discharge or to perform and, at common law, the loss resulting from the termination lies where it falls.

24.17 However legislation has been enacted to overcome the harshness of the common law particular. In NSW, the *Frustrated Contracts Act 1978* (NSW) provides a scheme for adjustments to be made to the parties' positions by way of apportionment (sharing) of loss caused by frustration.

24.18 In South Australia, the *Frustrated Contracts Act 1988* (SA) limits the effect of the common law, providing that a contract is not wholly frustrated if the frustrated part of the contract can be severed (removed) from the remainder of the contract. The Act also provides for actions for damages.

24.19 In Victoria, the *Australian Consumer and Fair Trading Act 2012* (Vic) enables the recovery of money paid and account to be had of expenses incurred and benefits obtained.

CHAPTER 6 – REMEDIES

25. Overview

25.1 The previous Chapter considered how contracts can be terminated. This Chapter examines what remedies might be granted if a contract is breached.

25.2 The types of remedy available depend on the nature of the breach of contract. This Chapter covers:

(a) Damages;

(b) Restitution; and

(c) Specific performance and injunctions.

26. Damages

26.1 Whenever a party to a contract (the defendant) breaches that contract, the other party (the plaintiff) will be entitled to an award of damages as monetary compensation for the breach.

26.2 Damages for breach of contract fall into a number of categories.

Compensatory damages

26.3 Damages for breach of contract can be *compensatory.* This means that - where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same position with respect to damages, as if the contract had been performed.

Expectation and reliance damages

26.4 A non-defaulting party may also seek *expectation damages*. Expectation damages compensate the plaintiff for the benefit he or she expected to gain from performance of the contract but has lost by reason of the breach.

26.5 Expectation damages are often described as damages for loss of profit, however this does not imply that no damages are recoverable either in the case of a contract in which no net profit would have been generated or in a contract in which the amount of profit cannot be demonstrated.

26.6 A plaintiff may also seek *reliance damages.* Reliance damages may be awarded where a plaintiff cannot establish his or her expectation loss. If the performance of a contract would have resulted in the plaintiff, while not making a profit, nevertheless recovering costs incurred in the course of performing contractual obligations, then that plaintiff is entitled to recover damages in an equal amount to those costs

26.7 Further, where it is not possible for a plaintiff to demonstrate whether or to what extent the performance of a contract would have resulted in a profit for the plaintiff, it will be open to a plaintiff to seek to recoup expenses incurred.

26.8 Both expectation and reliance damages are based on the central principle that a plaintiff is not entitled to be placed in a superior position to that which he or she would have been in had the contract been performed.

Case study: *McRae v Commonwealth Disposals Commission* (1951) 84 CLR 377

As set out above, McRae won a tender from the Commonwealth Disposals Commission to retrieve an oil tanker from a reef. However, when McRae went to retrieve the tanker, he discovered that the tanker did not exist.

The High Court recognised two categories of damages: the non-delivery of the goods purchased (the tanker) and the wasted expenditure in looking for it.

The Court held that the steps that McRae took in looking for the tanker were reasonable, and were the very course that the defendant would naturally expect them to take. Moreover, the wasted expenditure flowed from the defendant's breach.

Case study: *Bellgrove v Eldridge* (1954) 90 CLR 613

In an action for damages for breach of contract brought by a building owner against a builder, it appeared that the builder had substantially departed from the specifications and that, by reason of that departure, the foundations were defective, and the building was unstable.

The High Court held that the measure of damage was not the difference between the value of the building as erected and the value that it would have borne if erected in accordance with the contract but the cost, in excess of any amount of the contract price unpaid, of reasonable and necessary work to make it conform to the contract.

The Court also accepted that, in the circumstances, demolition of the building and rebuilding was reasonable and necessary to provide a building in conformity with the contract.

Limitations on the award of damages

26.9 In order to be awarded damages, a plaintiff must also show a causal connection between his or her loss and the breach of contract. That is, the plaintiff must establish that the defendant's default *caused* the damage suffered.

26.10 Further, the damage must not be *remote.* Damages will only be awarded where the loss arises naturally from the breach of contract. Further, the loss must be within the reasonable contemplation of the parties as a probably result of the breach.

26.11 In addition, a party must take reasonable steps to *mitigate* his or her loss. This means that if a party has an opportunity to limit the extent of his or her loss, he or she must take reasonable steps to do so. For example, if a builder fails to complete the building of a property that he or she has contracted with A to build, A is not entitled to let the land fall into disrepair if A has a reasonable opportunity to complete the building of the property and limit his or her losses.

27. Restitution

27.1 Separate from damages is the remedy of *restitution.* The rationale for restitution is in many cases the concept of *unjust enrichment.*

27.2 In the case of a terminated, but previously valid, contract, unjust enrichment occurs where work has been performed, but a right to payment has not yet accrued. Restitution is not compensatory in nature but rather is determined according to the benefit that the defendant has received.

27.3 The concept of unjust enrichment is best explained by reference to a specific example. In *Mann v Paterson Constructions Pty Limited* [2019] HCA 32, the Manns had contracted Paterson Constructions to build two townhouses pursuant to a domestic building contract.

27.4 Before the completion of the second townhouse, the Manns orally requested 42 variations to the townhouses during the period of construction. Paterson carried out the variations but did not give written notice according to the process under the contract. At the time that Unit One was handed over, Paterson told the Manns that there was around $48,000 to be paid for the oral variations, and the Manns refused to pay. Paterson then refused to continue carrying out construction until the variation amount was paid.

27.5 The Manns claimed Paterson refused to return to site until the bill for the additional work was paid, and that the work was defective. The Manns claimed that Paterson's conduct amounted to repudiation of the contract, and purported to terminate.

27.6 There were three different kinds of claims in respect of which Paterson sought restitution:

(a) Work done in respect of the contract for which Paterson had accrued a contractual right to payment at the time of its termination;

(b) Work done in respect of the contract for which Paterson had not yet accrued any contractual right for payment at the time of termination; and

(c) Work done in respect of the variation requests.

27.7 In respect of the *second* category, Paterson did not have a contractual right for payment. However, having carried out the work, the builder had incurred costs, including in relation to the building materials. The law of damages in contract law does not assist a person in the position of the builder. Therefore, restitution may step in to provide a just outcome.

27.8 A majority of the High Court held that, to the extent that a contractor will only become entitled to payment if works are wholly completed, or has not accrued the right to payment in respect of a portion of the works, the contractor may recover in *restitution*.

28. Specific Performance and Injunction

28.1 There are two other key remedies available for breach of contract: (1) specific performance, and (2) injunction. Both are *equitable* remedies.

28.2 Specific performance is an order by the court directing a contracting party to perform his or her obligations under the contract. Specific performance is only available as a remedy where damages are an insufficient remedy.

28.3 A common scenario where damages may be considered inadequate, and specific performance ordered instead, is a contract for the sale of land, particularly where the land has unique features.

28.4 In contrast, the remedy for breaches of contracts for the sale of goods or contracts for money will more often be damages.

28.5 The Court may also order an *injunction* to prevent breach of contract. An injunction is an order or judgment by which a party to an action is required to do or refrain from doing a particular thing. Injunctions are either prohibitory or mandatory and are either interim (interlocutory) or perpetual (final)

28.6 A common example is in the case of a restraint of trade in an employment contract. Where, for example, an employment contract prevents an employee from working for a competitor, a Court may order an injunction to prevent the employee from commencing work with a competitor.

28.7 A Court may order an injunction on an *interlocutory* basis. This means that the injunction is ordered on an interim basis, to preserve the status quo, prior to the final resolution of the matter.

28.8 In order for the Court to grant an interlocutory injunction, it must be satisfied of the following:

(a) There is a *serious question to be tried*. This involves consideration of the nature and strength of the plaintiff's case. The Court is unlikely to grant an injunction if the plaintiff is unlikely to succeed at final hearing.

(b) There is a risk of *irreparable harm* if the injunction is not granted. In the example above, the risk from a former employee commencing work with a competitor is irreparable, as the employer would be unable to prevent the passing on of trade secrets and so on.

(c) The balance of convenience favours the grant of the injunction. The Court here considers a myriad of factors that go to the necessity, utility and fairness of granting an injunction, including the potential harm in doing so.

28.9 A party seeking an interlocutory injunction must offer an *undertaking as to damages.* This means that they must undertake to pay for any damage arising as a result of the injunction.

28.10 A permanent injunction is a final settlement of the parties' rights and lasts indefinitely unless it is restricted by the terms of the order or dissolved by a further court order. A court will only grant a permanent injunction once it has made a final determination after hearing the matter at trial. The applicant must demonstrate the elements of the breach of contract and the prospect of continuing or recurrent injury.

CHAPTER 7 – FURTHER READING

28.11 Some further resources are available here:

Textbooks

- Contract law in Australia (J W Carter)
- Commercial Law: Commentary & Materials (G Pearson et al)
- Cases and materials on contract law in Australia (G Tolhurst & E Peden)

Websites

- *Contracts & Agreements*, published by the ACCC:

  https://www.accc.gov.au/consumers/contracts-agreements

- *Contracts*, published by Fair Trading NSW:

  https://www.fairtrading.nsw.gov.au/buying-products-and-services/guarantees,-contracts-and-warranties/contracts

- *Consumers*, contracts, the internet and copyright, published by The Law Handbook 2020:

  https://www.lawhandbook.org.au/2020_07_01_01_what_is_a_contract/