PART X – INCORPORATION

I EXPRESS TERMS

A *General Principles*

In addition to within the agreement itself, express terms of a contract may be found in:

- Pre-contractual communications
- Notices or documents provided in addition to the contract
- Signs displayed at business premises of one of the parties

To be a term of the contract, the term must be promissory in nature (*Oscar Chess*). The law draws a distinction between representations, which are not contractually enforceable, and warranties or promises, which are contractually enforceable.

B *Warranties versus Representations*

Whether a statement is promissory or representational depends on the intention of the parties. The question is decided objectively on the facts.

Test (from *Hospital Products v USSC*):

> *Would the statement reasonably be considered to be a promise by a reasonable person placed in the situation of the parties?*

The fact that a statement induced the other to enter into the contract does not make it into a promise (*Oscar Chess* per Denning LJ).

In general, three factors feature in judicial decisions about whether a statement is promissory in nature:

1 The language used by the parties

2 The relative experience of the parties

3 The importance of the statement

In reaching a conclusion, the term is examined objectively: would a reasonable person see it as a promise?

1 *Language*

The linguistic form of the statement will have a bearing on whether or not it should be regarded as promissory. However, statements expressed in factual rather than promissory terms can still be warranties if they are clearly promissory in substance (*Oscar Chess* per Denning LJ).

So, for example, representations couched as estimates or guesses may not be regarded as promissory, but guarantees may well be regarded as such. Note, however, that the statement-maker need not use the word 'promise' or 'warranty' in order to be making a promise (though such a statement would certainly indicate the existence of a term).

In a commercial context, statements may still be promissory even if they are couched in factual or descriptive language. The seller may be impliedly promising that the contents of the sale conform to the factual description given (eg, 'this car can go at this speed').

2 *Relative expertise of the parties*

The relative knowledge or strength of the parties may be relevant in assessing whether a statement was made as a promise.

This is not a subjective factor; the experience of the representor only affects how a reasonable person would interpret their intention (ie, to what extent the alleged promisor is presumed to be correct).

A statement made by a party with expertise to a person who is inexperienced is more likely to be promissory than a statement made by an inexperienced party (*Oscar Chess* per Lord Denning).

Oscar Chess v Williams:

Facts

- W offered to trade in his mother's car to a car dealer
- W described the car as a 1948 car as this was the date shown in the car's registration book (which had been fraudulently altered by the previous owner unbeknownst to W or his mother)
- On this basis, the car dealer paid Williams £290 for the car
- It turned out that the car was a 1939 model and, therefore, only worth £175
- The car dealer claimed damages of the difference in value (£115)
- In order to be contractually entitled to the £115, the dealer had to establish that W's statement (about the age of the car) was a term of the contract (and not merely a representation).

Issue

- Was W's statement that the car was a 1948 model a warranty to that effect, or was it merely a representation?

Reasoning

- There are different uses of the word warranty:
  - As a binding promise (ordinary English meaning)
  - As a subsidiary (non-essential) term in the contract
  - As an affirmation at the time of the sale
- Denning LJ:
  - Applies an objective test
  - 'Would an intelligent bystander reasonably infer that a warranty was intended?'
  - The existence of a warranty is not solely determined by the importance of the term to the contract
  - Instead, the enquiry looks at the reasonable person interpreting the term

- If the representation had been made by the car dealer when selling the car to a consumer, the result may have been different:
    - If the seller of car was a dealer, his statements to a buyer are more likely to be regarded promissory, owing to his relative experience
    - Here, W has no knowledge or expertise and was just stating a belief
    - A car dealer should have been able to tell the age of the car

Decision

- W's statement was a mere representation
- The dealer was more experienced, and should have known the car's model
- The relative inexperience of the statement-maker suggests that a reasonable person interpreting the statement would not regard it as a promise to the dealer

3 *Importance of the statements*

A statement which the circumstances show was highly significant or important to the transaction is more likely to be regarded as a promise than a statement of lesser significance: *van den Esschert*.

Hospital Products v USSC:

Facts

- USSC manufactured and sold surgical stapling equipment
- B, USSC's New York distributor, accumulated large stocks of demonstration products
- In 1978, B visited Australia and found out that the products were not patented
- On his return to the US B suggested to USSC that he should be appointed the exclusive Australian distributor in place of the existing distributor
- In November 1978, B met with USSC and made a series of statements about the potential of the Australian market and his suitability to effectively exploit it
    - USSC argues these are express terms
    - However, they were not very detailed
- On 27 December 1978 USSC wrote to B appointing him as the exclusive Australian distributor
- B signed and returned the letter to communicate his acceptance of the offer. As a result, the terms of the letter became express terms of the agreement between B and USSC
- B then acquired a large quantity of samples and sold them for himself on the Australian market in competition with USSC's products. He also deliberately deferred orders made to USSC so that he could fulfill them himself
- USSC sued for, inter alia, breach of contract. However, to be successful in its contract claim it had to establish that the statements at the meeting were terms of the contract
- The November 1978 statements:
    - that there was a great potential market for USSC surgical stapling products in Australia which was not being tapped by the existing distributor;
        - Doesn't use language of promise
    - that with his long experience and marketing knowledge he could do an outstanding job
        - Doesn't use language of promise
    - that this would be a great opportunity for him and USSC
        - No certainty
    - that he would set up a marketing organization with trained sales representatives
        - Promissory

- that after he got USSC's business up and running he might take on other non-competing product lines
  - Representation, but implied promise not to compete
- that because establishment of the business would take some time he would need financial assistance
  - Representation

Issue

- Can the November 1978 statements made prior to the formation of the contract be incorporated as express terms?

Reasoning

- The Court applies an objective test; the incorporation of the terms depends on

  > *whether the representations would reasonably be considered, by the person to whom they were made, as intended to be contractual promises; and if that person intended to accept them as such*

- Dawson, Wilson, Mason and Deane JJ
  - Of the November statements made, four are promissory:
    - That B would establish a marketing organisation
    - That B would devote his best efforts to distributing USSC
    - That B would not deal in Australia in competitive products
    - That B would not deal in Australia in other products in such a manner as would diminish his efforts to distributing the product
- Gibbs CJ:
  - Reaches a different conclusion of fact; however, there is no disagreement about which is the relevant test to apply
  - Ignores USSC's reliance on B's statements; instead, considers the question: 'what would a reasonable person think about the statements that were made?'
  - Of the November statements, only one was a warranty:
    - That B would set up a marketing organisation
- Whether a statement is promissory is a question of fact
  - Be sure to note the uncertainty of any particular conclusion being reached

Decision

- The Majority held that, because of B's subsequent competitive conduct and his failure to use 'best efforts' in distributing USSC's products, he was in breach of an express term of H's agreement with USSC

II MANNER OF INCORPORATION

A *Unsigned Documents*

The law draws a distinction between signed and unsigned documents.

In unsigned agreements, parties may attempt to incorporate terms by:

- Delivering a document containing terms to the customer
- Displaying terms on some form of sign at its business premises

Whether such conduct effectively incorporates the term will depend on two factors:

1 *Timing* (must be before formation since terms cannot be added afterward)

2 *Knowledge or notice* (promisee must have actual or reasonable notice of the term)

The onus of establishing an incorporated term rests on the plaintiff. However, where a defendant seeks to deny liability by incorporating a limiting term, they bear the onus of establishing that the term limiting liability forms a part of the contract.

1 *Timing*

No matter how promissory, if a statement is included after the contract has been formed, it cannot be a term. Notice must have been given before the contract was formed (*Oceanic Sun Line v Fay*).

Oceanic Sun Line v Fay:

Facts

- F made a booking for a cruise of the Greek islands
- Upon paying the fare, F was given an 'exchange order' which stated that it would be exchanged for a ticket on boarding the ship.
- When exchanged (issued) the ticket contained a 'Governing Laws' provision which provided that the courts of Greece should have exclusive jurisdiction on any action against the owner (clause 13).
    - This made it harder to sue Oceanic, since F would need to do so in Greece
- F was injured on the cruise and sued the owner for negligence in the NSW Supreme Court (obviously, not a court in Greece)

Issue

- Is clause 13 an express term of the contract?

Reasoning

- If the contract between F and O was made when the booking was made, then clause 13 could not be incorporated, because it was only when boarding the ship that the notice was delivered
- If, on the other hand, the contract was made when the 'exchange order' was exchanged for the ticket (in Greece), the term could be incorporate
- The reasonable person would see booking as contractually binding, so that is the cut-off point for incorporating terms
    - Similar to *MacRobertson Miller*: if the ship does not run, a refund is not necessarily offered
    - However, unlike *MacRobertson Miller*: the contract is formed upon booking, not boarding
- Special rules are applied to terms limiting liability:

- Shellar J in *Toll v Alphapharm*: a more stringent approach is adopted in when dealing with indemnity clauses
- These operate to attach causes of action against the promisor to the promisee as joint-defendant

Decision
- Clause 13 is not a term of the contract because it was delivered in a document at a point in time after the contract had been formed

2 *Knowledge or notice*

To be bound by delivered or displayed terms, the promisee must have one of:
- Knowledge of such terms (subjective); or
- Reasonable notice of such terms (objective)

Reasonable notice can be given in one of two ways:

- Notice by document:

  If a reasonable person would expect the document to contain the terms of the contract, the mere presentation of the document is likely to suffice. However, this may not apply to standard form contracts.

- Notice not contained in document:

  The party seeking to incorporate the terms must take reasonable steps to bring the terms to the notice of the party to be bound. What is reasonable will depend on the circumstances.

B *Signed Documents*

The general rule is that a party who signs a contractual document is normally bound by the terms set out in the document, even if he or she has not read the document and has no knowledge of its contents (*L'Estrange v Graucob*).

L'Estrange v Graucob:

Facts
- L purchased a cigarette vending machine from G
- As part of the transaction L signed a form headed 'Sales Agreement'
- L brought an action for damages for breach of an implied warranty that the machine was reasonably fit for the purpose
- G relied on a clause in the 'Sales Agreement' excluding all implied warranties as a defence to L's claim
- L claimed not to have read the term

Issue
- Can the exclusion clause operate even where L was not aware of the term?

Reasoning

- The following factors mitigate towards a finding in favour of G:
    - L had put her signature on the document
    - There is nothing suggestive of fraud on the part of G
    - L's lack of knowledge is solely as a result of her laziness; if a party is concerned about exclusion clauses, they should read them

- There may be a policy component to this decision:
    - When a promisee signs a contract, the promisor should be able to rely on the terms of that contract being enforced
    - Law and economics school: certainty is demanded of written contracts so as to enable efficient business transactions

- Was the clause in question one that the plaintiff should reasonably expect to be in such a contract?
    - Yes, it was a sales agreement relating to the vending machine
    - Note: do not assume that, just because the outcome is somewhat unfair, estoppel automatically applies; here, it doesn't, because there is no inducement

- The promisor is under no duty to bring clauses to the attention of the signing party (and nor should they be)
    - Business efficacy and certainty could not be achieved if every clause had to be brought to the signing party's attention
    - Such a requirement could also contravene the intention of the signing party, who may wish to waive the promisor's duty to them so as to proceed with the bargain more expeditiously
    - Possible exceptions to this strict approach:
        - *Toll v Alphapharm*
        - Standard form contracts

Decision

- Yes, implied warranties are excluded by the clause – even where the promisee has not read (but has signed) the document and is not aware of its terms

Toll v Alphapharm:

Facts

- RT was the Australian importer of a drug that was extremely temperature sensitive
- RT asked T to provide a quotation for transportation and storage of its drug
- RT was asked to, and did, sign an 'Application for Credit'
- The front of the application included the statement 'please read 'Conditions of Contract' prior to signing
    - RT did not read the conditions
- The terms set out on the back of the Application for Credit exempted T from liability for loss and contained a clause whereby RT agreed to indemnify T for loss or liability to others
    - This means that RT must pay damages for a successful action by A against T
- RT then engaged T to carry a supply of the drug to A by an additional contract of carriage
    - This is a separate contract of carriage
- T negligently held the drug at an incorrect temperature
- A sued T

- T sought indemnification from RT. This claim was based on the indemnity provision in the Application for Credit

Issue

- Can T rely on the indemnification clause to prevent A suing on the contract of carriage?

Reasoning

- The indemnity clause is held not to form part of the contract between RT and T
  - T had not done what was reasonably required to bring the clause to the attention of RT
  - The contract of carriage between T and A is a different contract to the Application for Credit between RT and T

- Shellar J:
  - The principle in L'Estrange is not black and white
  - Here, there is not a single contract, but 2 separate contracts (one of distribution and one application for credit)
  - The indemnity clause was not in the main contract, so T had an obligation to bring the clause to RT's attention
  - The 'application for credit' form contained a disclaimer of a very large scope; this was not reasonably to be expected, and notice of it needs to be given to RT

- The decision turned upon reasonable notice:
  - Where a clause is in a different document and not one to be reasonably expected, the promisor must ensure that the promisee is given reasonable notice of it

- What would you advise T to do in order to ensure its customers indemnify it against such loss in the future?
  - Bring the clause to each customer's attention
  - Alternatively, expressly exclude liability to the consignee in the main contract

- What is the effect of the decision on the rule in *L'Estrange*?
  - Not reading an indemnity clause in a contract of carriage is still no excuse, but where the clause occurs in a separate contract (in a location not reasonably to be expected), the promisor is required to give reasonable notice to the promisee of its existence

- Can the decision be reconciled with the view of Brennan J in *Oceanic Sun Line*?
  - Yes; here, unlike in *Oceanic Sun Line*, the alleged term is not in the same contract as the one being sued on for breach

Decision

- Because T had not given reasonable notice to RT of the existence of the indemnification clause in the application for credit, the term does not form a part of their contract of carriage and T is liable to A in damages

Note that contracting parties cannot exclude all liability under a contract. If that were possible, the promise made by the promisor would be illusory, as there would be nothing to compel them to perform their obligations (which are essentially nugatory). Thus, terms which minimise liability are more correctly referred to as 'limiting terms', since they can only ever limit – and not completely exclude – liability (*MacRobertson Miller Airline*).

III STANDARD FORM CONTRACTS

A *Definition*

The express terms of a contract are not usually negotiated between the contracting parties. In fact, 99% of written contracts are made on the basis of a standard form contract supplied by one of the parties.

Suppliers (and sometimes acquirers) are often prepared to supply (or acquire) goods or services only on the basis of their own standard terms. Contracts made on this basis are often referred to as 'contracts of adhesion'.

Traditionally, standard form contracts are – like normal contracts – binding records of express terms. This result is derived from *L'Estrange*, which stipulates that a party who signs a contractual document is normally bound by the terms set out in that document, even if he or she has not read the document and has no knowledge of their contents.

However, this rule has been criticized in cases such as *Toll v Alphapharm*. It may operate even more harshly in the context of standard form contracts, where the parties are often separated by a large differential in resources and negotiating power, and promisees rarely read and fully understand every term in the agreement.

Tilden Rent-A-Car v Clenndenning:

Facts

- C entered into a car rental agreement with T pursuant to a standard form agreement
- The agreement denied insurance coverage in respect of damage suffered while the car was operated in any breach of the law or breach of the agreement
- The fine print of the agreement contained a clause prohibiting a person operating the car if they had consumed alcohol (even if they were still within the legal limit)
- C was involved in a collision.
- Prior to the collision C had been drinking but was within the legal limit and was able to show that the accident was not caused by intoxication
- T sued C in respect of damage to the vehicle [???] resulting from the accident, alleging breach of contract

Issue

- Is the clause prohibiting consumption of alcohol before driving the vehicle a part of the contract, even though C had not read it?

Reasoning

- The Court of Appeal recognised an exception to the rule in *L'Estrange*
- Where a promisee has signed a contract, terms will not be incorporated without the promisee's knowledge thereof in situations where:
    - A standard form contract contains 'stringent and onerous provisions'; and
    - The document has been signed without being read or understood; and
    - The party seeking to rely on the contract knows, or ought to know, that the signature does not represent the true intention of the signor

- In such circumstances, the stringent and onerous terms are enforceable only if the drafting party has taken reasonable measures to bring the terms to the attention of the non-drafting party
    - This approach suggests that abnormal clauses in fine print should be required to be brought to the promisee's attention in certain situations

Decision

- On the facts, it is clear that:
    - The clause in question was a 'stringent and onerous provisio[n]'
    - The agreement was a standard form contract
    - The document was signed by C without reading the clause
    - T knows that, not having read the contract, C's signature does not represent his true intention

- An exception to the rule that terms are incorporated into signed contracts whether they have been read by the promisee or not (*L'Estrange*) operates in favour of C
- T cannot recover for breach of contract from C, because C has not breached any of the other terms of the agreement

The decision in *Toll v Alphapharm* indicates that where a term is introduced in an unexpected way (in a secondary contract) it is less likely to be incorporated into the main contract. Though this isn't quite the same as the *Tilden* principle, both decisions highlight an increased judicial awareness of injustice arising out of strict application of the *L'Estrange* rule.

Differences between *Toll* and *Tilden*:

- In *Toll*, there is a second contract from which the term is alleged to be drawn, whereas in *Tilden* there is only a single contract of lease
- In *Toll*, the Court's objection to incorporation pertains to the unexpected manner of incorporation of the term and the lack of reasonable notice (though the wide nature of the indemnification is also likely to have been factored into their analysis)
- In *Tilden*, the objection stems from the abnormal/stringent nature of the term and the promisor's knowledge that the term has not been read/assented to

B *Justifications and Criticism*

Kessler (1943) has observed that standard contracts are typically used by enterprises with strong bargaining power and that the contractual intention of the weaker party is subjugated to that of the stronger party, who dictates the terms.

Hillman & Rachlinski (2002):

- Benefits arising from the use of standard form contracts:
    - Economy of scale
        - 1 contract for all means that the legal costs involved in writing the contract are spread over all consumers (parties to the contract)
    - Risk allocation
        - Economics dictates fair distribution of risk
        - Consumers will, in a perfect market, realise if the provisions are unfair and consume elsewhere
    - Savings in litigation expenses
        - Quicker to litigate identical contracts

        - Not ambiguous since regularly encountered

- Possible reasons why consumers don't read standard form contracts:
    - Consumers recognise the futility of attempting to negotiate with large companies, so they don't
    - Consumers don't understand the terms
    - No-one is available who is able to explain the terms
    - Consumers have faith in legal standards to protect them from malicious corporations
    - Competitors are likely to have the same/similar terms
    - Consumers assume the terms won't apply to them and cannot anticipate possible implications

- In the perfect market, global market forces regulate fairness in standard form contracts by influencing consumer decisions about where to enter into a contract; if a provision is unfair, consumers will go elsewhere; this means that in order to stay competitive, a standard form contract will need to embody a base level of fairness in order to gain consumer support
    - Economists idealise such a scenario, because external regulation is a barrier to efficiency
    - Market self-regulation allows for resources to be put to their most valuable use and reduces transaction costs
    - In this case, a minimum level of fairness in a standard form contract would be retained so as not to divert resources elsewhere or increase costs through litigation by unhappy consumers
    - However, the present market is not perfect, and the fairness of standard form contracts varies quite widely
    - If the market will, ideally, observe boundaries of its own accord, this minimum standard of fairness might as well be set by the legislature – the resulting certainty and uniformity may well be more efficient than *ad hoc* determinations of fairness

- Problems with standard form contracts:
    - Promisees often bound by something they have not read or understood
    - Free rider problem: it is not worth an individual consumer's time to read a standard form contract, but if everyone did, the companies would have to ensure that they were fair
    - Cost measurement
    - They lead to the conclusion by consumers that negotiation is impossible; consumers are increasingly submitting to the will of the stronger party rather than reaching a genuine bargain
        - Is non-negotiability a problem?
        - Who should fix it – the courts or the legislature?
    - Pressure to sign rather than read: reading signals distrust, other people might be waiting in line, the consumer may be dissuaded by the vendor, etc
    - To be concerned with the terms is considered an irrational response: rational people should be happy with the lowest price, and would not consider risks or other factors as additional costs

- Do these problems justify a change of approach?
    - The consumer looks at the cost of reading a standard form contract (time, effort), and offsets this against the benefit of reading it (since not free to negotiate or go elsewhere, no benefit); the cost outweighs the benefit, so it goes unread
    - While standard form contracts aren't necessarily as true an expression of a completed bargain than contracts drafted and negotiated by both parties, assent

to the terms of a standard form contract is not problematic unless the signing party is compelled to do so
    - The role of statutory provisions in limiting unfair provisions in consumer contracts should be the minimum required to protect consumers, who should – at least in theory – be able to consent to any terms they wish; economically, the a less regulated market will also perform better whilst reaching its own equilibrium of fairness

- Economists: do not regulate the market; allow the market to regulate itself by global forces effected by rational agents in pursuit of utility maximisation
    - There is no incentive to modify contracts for the few people that do read it; market forces (eg, the media) hold companies accountable to fair (or at least similar) standards

- The courts are right to treat standard form contracts with suspicion; they are a necessary part of modern consumer transactions, but have the potential to cause injustice

- The general failure of consumers to read standard form contracts is not a problem so long as the contract does not contain unfair provisions – if a legislative solution (such as the *Fair Trading Act*) is effective at preventing unfair terms from being added to contracts, then consumers will be further dissuaded from reading, since they know that if something is unfair it can be excluded

- The common law is ill-equipped to deal with the problems associated with standard form contracts:
    - The basis of contract law is genuine consent to a bargain; signing standard form contracts, however, means that the terms of the bargain are not devised by both parties
    - Common law rules relating to reasonable notice and incorporation of terms have not been sufficiently altered in response to the realisation that many bargains are today the product of only one party's intention, and that this party is usually the stronger and richer one
    - By holding relatively weak promisees to terms they don't understand and most likely have not read, common law rules of contract have the potential to produce unjust outcomes, regardless of any theoretical motivations on which the doctrine is based

- Contracts entered into over the internet raise several additional concerns:
    - People spend even less time reading the conditions
    - Many minors become parties to electronic agreements
    - It is difficult to bring to reasonable notice electronic terms in an agreement, unless the 'signing' is conducted in person
    - The ease with which electronic agreements can be accessed and assented to means promisees don't necessarily treat them with the same degree of seriousness as paper standard form contracts, despite giving rise to similar (or even more onerous) obligations
    - Because the terms are fixed on screen, and the other party is often not contactable (as opposed to merely unwilling to negotiate), signing parties have even fewer opportunities to modify or query terms

C *Unfair Contracts*

Last year, new provisions were introduced into the *Fair Trading Act 1999* (Vic) regulating unfair consumer contracts.

The main provisions permit consideration of how they may impact on standard form contracting practices that effectively require the consumer to 'take it or leave it'.

Fair Trading Act 1999 (Vic) – Part 2B:

s 3 A consumer contract is

> *an agreement, whether or not in writing … to supply goods or services of a kind ordinarily acquired for personal, domestic or household use or consumption, for the purpose of the ordinary personal, domestic or household use or consumption of those goods or services.*

s 32W Definition of an unfair term:

> *a term in a consumer contract is to be regarded as unfair if, contrary to the requirements of good faith and in all the circumstances, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer.*

s 32X Assessment of unfair terms

- whether term was individually negotiated
- whether term is a proscribed term
- whether the term has the object or effect of:
  - ❑ permitting the supplier but not the consumer to avoid or limit performance of the contract (one sided exclusions or indemnities);
  - ❑ permitting the supplier but not the consumer to terminate the contract;
  - ❑ penalizing the consumer but not the supplier for a breach or termination of the contract;
  - ❑ permitting the supplier but not the consumer to vary the terms of the contract;
  - ❑ permitting the supplier but not the consumer to renew or not renew the contract;
  - ❑ permitting the supplier to determine the price without the right of the consumer to terminate the contract;
  - ❑ permitting the supplier unilaterally to vary the characteristics of the goods or services to be supplied under the contract;
  - ❑ permitting the supplier unilaterally to determine whether the contract had been breached or to interpret its meaning;
  - ❑ limiting the supplier's vicarious liability for its agents;

- ❑ permitting the supplier to assign the contract to the consumer's detriment without the consumer's consent;
- ❑ limiting the consumer's right to sue the supplier;
- ❑ limiting the evidence the consumer can lead in proceedings on the contract; and
- ❑ imposing the evidential burden on the consumer in proceedings on the contract.

s 32Y Effect of unfair terms

- unfair terms in consumer contracts are void
- prescribed unfair terms in standard form contracts are void
- the contract will continue to bind the parties if it is capable of existing without the unfair term or the prescribed unfair term

- Does the contract contain other terms you think are unfair that do not fall within the s 32X list?
- Are there other problems with standard form contracts not addressed by Part 2B?

IV PAROLE EVIDENCE RULE

A *Role and Exceptions*

The parol evidence rule determined what evidence is available to the court to incorporate and construct contractual terms. The parole evidence rule has two parts:

- Construction – prevents extrinsic evidence being given to add to, vary or contradict the terms of a contract as they appear in the writing document (today);
- Interpretation – limits the evidence that can be given to explain the meaning of the terms of written contracts

1 *Justifications for the parole evidence rule*

The principle justification for excluding evidence of pre-contractual dealings in circumstances where the parties have formed a concluded bargain in writing is that, if antecedent evidence were allowed, it may have the effect of altering – whether by adding to or subtracting from – the terms to which both parties eventually agreed.

Courts may exclude evidence of earlier offers, negotiations, and circumstances generally in order to ensure that the terms of the contract as stated in its final form are given full effect (Denman CJ in *Goss v Lord Nugent*).

2 *Limitations upon the parole evidence rule*

The ambit of the rule is restricted by four qualifications or exceptions. In the following circumstances, or to demonstrate the existence of the following, the parol evidence rule does not apply:

i Contracts partly in writing

ii Collateral contracts

iii Rectification

iv Estoppel

B *Contracts Partly in Writing*

The parole evidence rule only applies to exclude evidence where a contract is wholly in writing (*Hoyt's v Spencer*).

A contract may be stated to be wholly in writing by using an 'entire agreement' or 'merger' clause. This is a broad exclusion of previous dealings, such as oral promises and evidence of prior agreements. It says that the present document is a complete record of the parties' agreement.

In the absence of entire agreement clauses there are two approaches to determining whether a contract is wholly in writing:

1 The rule is attracted by the production of a written document that appears to be a *complete record* – extrinsic evidence is not normally admissible; or
   i Only if the document looks incomplete is evidence allowed

2 The rule has no application <u>until</u> it is determined that the parties intended the document to contain all contractual terms
   1 This is the approach favoured by Australian courts

If the agreement is found to be wholly in writing, the parol evidence rule applies to exclude extrinsic evidence. If not, the evidence is admissible to show what additional terms, if any, should be incorporated.

When determining whether the contract is complete or partially written and partially oral, the Court looks for a fundamental hole in the formal contract between the parties. It must be established why the written document isn't complete (*Hospital Products v USSC*).

Hospital Products v USSC:

<u>Facts</u>

- See above (Part I, s B, ss 3)

<u>Issue</u>

- Given the letter of 27 December 1978, was evidence of the conversations admissible?

Reasoning
- The letter cannot possibly be the complete evidence of the agreement
- The bulk of the alleged promises were made during the earlier conversations
- Gibbs CJ:
  - Admitted on pleadings that the contract was partly oral, partly written
- Mason J:
  - Facts indicate that no formal contract was breached (the letter)
  - It is consistent with not entering into a further contract that the contents of earlier conversations were meant to be binding

Decision
- Because the formal contract doesn't contain details of any of the promises made by B, it is incomplete; evidence of the earlier conversations is admissible

SRA v Heath Outdoor:

Facts
- H entered into a number of contracts with SRA which permitted it to erect advertising signs on SRA premises for a period of 5 years
- The contracts contained a clause that permitted the SRA to terminate without cause by giving one months notice (clause 6)
- H was concerned about the lack of certainty the clause introduced and raised this with the representative of the SRA (G)
- G told H there was no need for concern but said it was difficult to alter the standard terms of the contract; G expressly told H that the only time that such a clause is ever invoked is for non-payment of rent or if someone wants to advertise objectionable content
- H signed the agreement and did not cross clause 6 out because G had indicated this would be problematic

Issue
- Can H introduce evidence to establish the existence of an oral clause?

Reasoning
- H attempt to attempt to invoke the exception to the parol evidence rule that applies where a contract is partly written and partly oral
  - If it could be proven that an oral term was introduced by G to the effect that clause 6 would not be invoked capriciously or without due cause, SRA would be in breach

- Williston (textbook writer):
  - When a document appears on its face to be a complete record of the parties' contract, it is conclusively presumed to be the entire agreement
  - Evidence cannot be admitted to prove otherwise

- Corbin (textbook writer):
  - The issue is whether the parties assented to a particular writing as the complete and accurate integration of the contract
  - Extrinsic evidence should be admitted to resolve this issue

- McHugh JA:

- Prefers Corbin's approach: admit evidence to determine whether the written document is complete or whether the contract has terms elsewhere
- On the facts, though there is evidence to support the statements made by G, it appears that the entire contract is within the written agreement
- The document was very thorough – there were no holes; this mitigates against invoking the exception to the parol evidence rule
- The agent (G) had no authority (and admitted this) to add terms or vary the contract in any way, so H cannot assume that clause 6 would not be enforced, nor can he attempt to introduce additional terms based on openly unauthoritative statements made by the agent

Decision

- Mr G's statements were incapable of giving rise to a collateral contract because he had no authority to make any additions or alterations to the contract of any kind
- Because the written contract is complete (was not added to in any way by G), the parol evidence rule applies to exclude evidence of H's conversation

C *Collateral Contracts*

A collateral contract is a contract where one party makes a promise in some way connected to, but independent from, the main contract.

When arguing that a collateral promise (such as a verbal agreement) is contractual, consideration is required in order for it to be enforceable. In most cases, consideration for that promise will be the promisee to the collateral promise agreeing to enter into the main contract.

For a statement to give rise to a collateral contract, the statement must:

1. Be made as a promise (*JJ Savage*)
    a. Cannot be an estimate or guess – these would be mere representations and lack sufficient certainty and intention to be contractual in nature
2. Be intended to induce entry into the contract (*JJ Savage*)
3. Be consistent with the terms of the main contract (*Hoyt's v Spencer*)

The parole evidence rule does not apply to exclude evidence of the collateral contract (*JJ Savage*).

JJ Savage v Blakney:

Facts

- B bought a boat from JJS
- Prior to agreeing to buy the boat B asked JJS' manager to write down information about various engines
- B's decision to buy a single diesel engine rather than a twin diesel engine was made as a result of JJS' manager informing him that the estimated speed of the boat with that motor would be 15mph
- There was no reference in the contract executed to the capacity of the boat to obtain a particular speed
- The boat supplied was not capable of moving faster than 12mph

- B sued for breach of contractual warranty, alleging that the representation of the estimated speed of the boat was a condition or warranty of the contract or that it was a collateral warranty

Issue
- Did the statement 'estimated speed 15 mph', contained in the appellant's letter, result in a collateral contract being formed?

Reasoning
- The Court is heavily influenced by the certainty of a contractual document
- There are three things the acquirer of the boat could have (and should, if the speed of the boat was really important to him, have) done:
    - Make reference to the speed somewhere within the contract of sale
    - Make the representation about speed a condition of the contract (so he could terminate without payment if it turned out to be false)
    - The buyer could also have formed his own opinion as to whether or not it would travel at 15mph
- The law already has mechanisms for enforcing these types of promises; it's the buyer's fault for not incorporating the speed of the boat as a term in the contract of sale

Decision
- No, the statement does not form a collateral contract, because it was not promissory and should not, as a matter of policy, be allowed to supplant the very obvious steps the plaintiff could have taken to ensure the representation formed a part of the written agreement

The terms of a collateral contract must also be consistent with the contents of the main contract. They cannot expressly contradict, and arguably cannot modify, the express terms of the primary agreement (*Hoyt's v Spencer*).

Hoyt's v Spencer:

Facts
- S leased premises to H for four years
- A written lease was entered into that provided that S might at any time terminate the lease without cause by giving 4 weeks notice in writing
- During the currency of the lease S gave notice and H gave up possession
- H then brought an action against S alleging that S had breached a promise in a collateral contract that he would not give notice to quit

Issue
- Did a collateral contract arise to this effect?

Reasoning
- H alleged that S had promised not to give notice to quit and that, in return, H had promised to enter into the lease

- The Court admitted evidence of the collateral contract, but refused to enforce it
    - H's entry into the lease could be consideration for a collateral contract with S (see *Heleynt Symonds*)
    - However, if a collateral contract is inconsistent with the main contract, the Court

will not enforce it
    - This effectively changes question of admissibility (law) to question of fact: consistency
    - In admitting evidence, there are two separate questions to consider:
        - Will the Court hear evidence?
        - Having considered the evidence, will it conclude that there is a collateral contract?
            - Can the main contract be viewed as consideration?
            - Is the statement alleged to constitute the collateral contract promissory in nature?

- Effectively, inconsistency is equated with unenforceability
    - H's promise to enter into the contract constitutes an agreement to accept all the terms – H should have sought to change the '4 week's to '3 months', or whatever was acceptable to it
    - If someone has made a pre-signing representation that a contractual clause will not be enforced, a collateral contract argument is <u>*very*</u> unlikely to succeed
        - <u>Unless</u>: the collateral promise *adds* to the contract
        - Even then, only the additional promises could be enforced – not the ones altering/in conflict with the main contract

<u>Decision</u>

- Though a collateral contract was made between H and S, it is unenforceable because it conflicts with the terms of the primary contract between them (which overrides the secondary terms)

Similarly, in *SRA v Heath Outdoors*, the representations alleged to be promissory could not have been enforced – even if a collateral contract had existed (which on the facts it did not) – because it would have been inconsistent with the terms of the written contract.

D *Rectification*

Extrinsic evidence is also admissible if its purpose is to show that the contractual document mistakenly omits or misstates the terms that were in fact agreed on by the parties.

There must be a common mistake (one which is unlikely to be admitted by both parties, particularly where a breach of the contract is at stake), not a misunderstanding by one party.

If terms have indeed been misstated or omitted, the court will 'rectify' the contract (*Pukallus v Cameron*).

Pukallus v Cameron:

<u>Facts</u>

- P purchased land from C
- The contract of sale described the land as 'Subdivision 1 of Portion 1154'
- Both parties believed that subdivision 1 included a bore and an area of cultivated land which they inspected together before the sale was completed
- In fact, the area in question was part of subdivision 2
- P sought rectification of the contract

Issue
- Can the Court rectify the contract to pertain to 'Subdivisions 1 *and* 2 of Portion 1154'?

Reasoning
- The Court admitted extrinsic evidence
  - The parol evidence rule does not apply when attempting to show rectification
- However, the Court refused to rectify the contract
  - The Court will not grant rectification where the parties would have used different words had they known the true facts
  - Here, the parties clearly intended to write 'subdivision 1' (ie, it was not a transcription error), so it was not a mistake – just a common misconception of *meaning*
  - This approach is partially influenced by the view that parties should double-check the important details of a contract (particularly where sale of land is involved)
- Because the contract only specifies 'Subdivision 1' as part of the sale, P cannot recovery damages for breach of contract
- However, the doctrine of mistake may apply to allow P to cancel (rescind) the contract without penalty

Decision
- Because the common mistake was one as to *meaning* (rather than a transcription error), the Court will not grant rectification and the terms of the contract stand

E *Estoppel*

Estoppel may also be used to establish the existence of an oral promise supplementing a written contract. The principal advantage of estoppel is that it is not restricted by the requirement of consistency with the main contractual provisions (*SRA v Heath Outdoors*).

However, the admissibility of the evidence required to mount an estoppel claim remains settled (*Whittet v State Bank of NSW*).

Whittet v State Bank of NSW:

Facts
- SB agreed to lend Mr W $100 000 in overdraft
- Mrs W agreed to permit the matrimonial home to be mortgaged (Mr and Mrs W were joint tenants) to secure the overdraft
- In fact, the mortgage was not limited to $100 000
- Mrs W's solicitor was aware of this and raised it with SB
- SB gave verbal assurances that it would not permit the principal sum of indebtedness to exceed $100 000
- SB suffered loss on certain foreign exchange transactions carried out on behalf of Mr W and sought to enforce the mortgage in its terms (ie to recover an amount higher than $100 000)

Issue

- Are SB's verbal assurances capable of giving rise to an estoppel such as to prevent them from recovering an amount greater than that represented ($100 000)?

Reasoning

- No collateral contract can exist:
    - This is because the representation ($100 000 limit) is inconsistent with the terms of the main contract (not limited to $100 000)

- The contract cannot be rectified:
    - There was no common mistake – both the bank and Mrs W's solicitor knew that there was no $100 000 limit to the bank's recoverable principal

- The decision was based upon estoppel:
    -
- Note the influence of policy:
    - For estoppel:
        - Fairness (consistent with *Walton Stores*)
        - Enforcement of promises made by the parties
        - *Logiane v Hately* (equitable principle operating alongside contract to give the minimum necessary to achieve justice)
        - Per Mason CJ and Deane JJ in *Walton Stores*:
            - 'It may be just as unconscionable to exercise a right acquired after a promise that such a right would not be exercised'
            - This is what SB has done in this case
    - Against estoppel:
        - Certainty/finality of written contract would be undermined
        - The Court does not want to have to consider evidence in every dispute of representations or prior claims made about the terms of the contract (floodgates argument)
        - Rolfe J (citing *Johnson Matthey Ltd v AC Rochester Overseas Corp*): the written contract would effectively be ignored in favour of prior dealings if an exception is recognised on the basis of a representation alone
            - Also noted that the integrity of the contract as a written instrument can be maintained by requiring 'clear and convincing proof'

- As a result of this decision, it is arguable that if estoppel can be relied upon in a situation such as this, there is no need to maintain 'collateral contract' and 'rectification' as alternative bases for the recognition of pre-contractual statements

- Per McLelland J in *Bentham v ANZ*: there are two main policy issues arising out of the widening of estoppel to establishing collateral contracts:
    - Reconciling with the parol evidence rule – ensuring finality of the written instrument and not undermining certainty
    - Whether the standard of proof required to raise an estoppel is as high as that required for rectification – at present, the level seems to be 'clear and convincing'

Decision

- Requiring 'clear and convincing proof' of the representation and the circumstances giving rise to the estoppel is sufficient to ensure the finality of the written contract
- Because the evidence is on these facts, clear and convincing, Mrs W is entitled to succeed against the bank, which is estopped from recovering more than the $100 000 principal as a result of their representation to that effect

Note also the decision in *Australian Co-operative Foods Ltd*, which dealt with, inter alia, an estoppel argument in the context of raising a collateral contract:

- The fact that the parties reduced their agreement to writing shows the relative weight they attributed to the terms – those written should be accorded more emphasis than those which remained verbal
- *SRA v Heath Outdoors* (per McHugh JA) and *Whittet* (per Rolfe J) do not give sufficient weight to the policy considerations of finality and completeness in the written document, which are undermined by granting an estoppel
- Evidence is often extensive, discursive, and inconclusive – even where demonstrative, it is of less value than the parties' 'considered written expression'
- 'Poorly based' attempts to establish pre-contractual estoppel are 'unfortunately common' – they are 'unuseful and very wasteful of resources' (floodgates)

V HYPOTHETICAL SCENARIOS

A *Exercise 12*

- Assume complete written contract
- Prima facie, the parol evidence rule operates to exclude prior evidence from complete, written contracts
- Run through the exceptions:
    - Partly written, partly oral?
        - Unlikely, since fairly complete
    - Collateral contract?
        - P promises to enter into the main contract in return for D's promise that the cloud point will be stored at a temperature not greater 30 degrees and with a concentration of fatty acid less than 1%
            - Promissory? Yes
            - Inducement? Yes, since trying to assuage P's hesitations about entering into the contract out of fear for the storage temperature and fatty acid content
            - Consistency? The collateral contract would add supplementary or additional terms, so would be consistent
                - But: oil is coming from another source, so asking to be crossed out

B *Exercise 13*

- Exceptions:
    - Collateral contract:
        - Promissory? No – gesturing to equip is hardly promissory in nature
        - Inducement? Probably
        - Consistency? Definitely not
    - Clause 27 excludes the partly oral, partly written contract scenario
        - The contract will be considered to be complete
        - This clause invokes the parol evidence rule

C *Exercise 14*

- Complete contract?
- Partly oral, partly written contract?
    - Would a reasonable person looking at the lease think it was complete?
    - Depends
    - Probably not incomplete
- Collateral contract?
    - Promissory? Yes
    - Inducement? Yes
    - Consistent? No – inconsistent with 'without reduction'
- Estoppel
    - Uncertain whether it will be recognised, but note: elements present
    - Reed doesn't require consideration