THE LAW BOOK COMPANY LIMITED

EXEMPTION CLAUSES AND IMPLIED OBLIGATIONS IN CONTRACT

BY JOHN LIVERMORE

FOREWORD

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The Hon Justice MD Kirby CMG
Chairman of the Australian Law Reform Commission

Principles and Pragmatism

By the time the reader gets to the last chapter of this book, he or she will not be surprised to find the author's lament that the current state of the law relating to exemptions clauses is 'unmanageably complex'.[1] If the reader has patiently read the twists and turns of case and statute law on the subject — mostly within the past two decades — he or she will be bound to agree. What is the law doing here? What are the policy choices which underpin the approach of the law to exemption clauses, exclusion clauses, indemnity clauses and other provisions inserted in contracts to help parties escape legal liability that might otherwise fall on them? Few judges, searching for that thread of Ariadne that will lead them through the maze of case and statute law, tarry to identify the deep undercurrents of public policy.

One exception to this judicial diffidence is to be found in the judgments of Lord Denning. They have been very influential in the area of the law covered by this book. They have not always carried the day. For example, his doctrine of 'fundamental breach' for many years provided a vehicle for avoiding unacceptable exemption clauses. It reigned supreme even after it was qualified in the Suisse Atlantique case.[2] However, the doctrine proved difficult to apply in practice, even as a tool for judicial analysis. The High Court of Australia quickly followed the Suisse Atlantique effort to beat a retreat which ultimately led the courts back to the actual language of the contract entered into between the parties.[3] Subsequently the House of Lords in the Securicor case[4] made it absolutely clear that there was no separate rule of law by which, regardless of their terms, exemption clauses were to be eliminated or deprived of their effect based upon Lord Denning's suggestion that 'fundamental breach' was a rule of law.[5] This question was henceforth to depend upon the construction of the whole contract.

Harsh exclusion provisions may perhaps have been included in printed forms. They may have been given little, if any, attention by the parties. They may have been presented by the contractually strong to the contractually weak. But the law should normally leave it to the parties to apportion the risks as they saw fit. In the real commercial world, they should be left to look after their own interests, perhaps by insurance. They should not be able to call in aid the uncertain application of a disqualifying rule of 'fundamental breach'.[6]

What are the underlying principles of the common law that have brought the highest courts in England and Australia to this conclusion? In 1979 Professor PS Atiyah wrote his important text, The Rise and Fall of Freedom of Contract.[7] This work elaborated an earlier thesis propounded by him in the Law Quarterly Review.[8] According to Atiyah, the conceptual presuppositions and the resulting rules of the 'classical' law of contract 'reflected a set of values and ways of thought' of the 19th century, and have become incongruous and even unacceptable in basic respects in contemporary society.[9] Atiyah called for drastic revision not only of the law of contract but also of those rules which distinguished a quasi-contract and contract from tort.

At about the same time, in his Inaugural Lecture for the University of Oxford, titled provocatively 'From Principles to Pragmatism'[10], Atiyah went out of his way to praise judicial pronouncements which were unrelated to the production of just results in the particular case before the court. The apparent inconsistency in the theses in his writings on contract and in his Inaugural Lecture of such an important writer in this area as Atiyah have been remarked by Julius Stone.[11] Atiyah's thesis in his Inaugural Lecture was also criticised by the late Sir Otto Kahn-Freund. According to Kahn-Freund, our legal system is to be seen as in the midst of 'an evolution of a more refined sense of justice'. We are, he declared, possessors of 'more highly developed criteria of equality and inequality':

> It means a reduction of that 'equality' of treatment of unequals which ignores differences between consumer contracts and commercial contracts, property for production and property for consumption, standard contracts and individual bargains — ... Our insight into what is 'unequal' is sharper today than it was in the time of Lord Ellenborough or Lord Eldon, or perhaps of Ricardo, and perhaps the insight merely reflects a keener sense of compassion and of humanity than was available to the generations which presumed to lay down rigid principles for a multitude of unpredictable situations.[12]

Here, then, is the germ of the issue that is dealt with in this book. Contractual relations are infinite in their variety. The parties may be quite unequal in their bargaining power. The terms of their contracts may be written or unwritten, clear or unclear, standard forms or individually negotiated oral arrangements. They may be made with exquisite care and precision. They may be made in an off-hand and thoughtless way, with little or no regard to the possibility that they will lead to a dispute and come before a court. The law of contract must evolve general rules. But those general rules may apply unequally and even unjustly in the fact situation of a particular case. A rule suitable to a great maritime and trading country (England) may not be appropriate for a large island continent, distant from its markets and dependent upon foreign shippers arriving at its coast presenting ready-made, standard contracts to be signed.[13] What may be 'reasonable' and 'just' as between commercial parties, able to look after their own interests, may not be 'reasonable' and 'just' when one party is an untutored consumer, relatively powerless in the enforcement of his claims. Whereas insurance may be available and appropriate as a means of self-protection or spreading the risk equitably in one case[14] it may not be reasonable to expect it in another. Whereas reliance upon an exclusion clause in one instance may strike the court as merely a legitimate definition of the agreed risk-taking, in another, it may produce a result that is denounced as outrageous.[15]

Law reform and restatement

The thread of Ariadne that runs through this book can be found. It is the reference to law reform. There are three reforming agencies at work. The courts have attempted reform. But the result has often been a denser maze. Lord Denning believes in achieving reform by the techniques of the common law: to deal with the instant case, to produce prompt change and to develop the law as judges have been doing for centuries. But though he has struck a number of notable blows recorded in this book[16], not all of them have succeeded in the end. In any case, we now live in the age of legislation. Increasingly, the role of judges is that of interpreting the reform legislation enacted by Parliaments. As this book shows, the legislatures have been busy in this area.

The original Sale of Goods Acts, copied throughout the English-speaking world, were framed at the end of the 19th century. Though the legislation had the merit of brevity and comparative clarity, the markets differed and they changed. The mass production of goods and services, higher standards of living and education, the advent of consumerism and changing patterns of trade, including world trade, all contributed to the need for broader legislation. Step by step, the legislators ventured upon the course. In Australia, the Trade Practices Act 1974 introduced important changes.

However, it was basically limited to contracts for the supply of good to a consumer by a corporation. There were large remaining areas to attract the experimentation of State legislators. That experimentation ensued. Much of it, like the Australian Trade Practices Act, was designed in such a way as to overcome purported efforts of exclusion by exemption clauses.

Among the most radical legislative reforms introduced was the Contracts Review Act 1980 (NSW) based broadly on a report by Professor John Peden.[17] The legislation is only now being tested in the courts. How the courts will strike a fair and reasonable balance between contractual terms and fairness in the individual case remains to be seen.

Sometimes the reforming legislation has been of a much more limited and specific character. Thus the Chattels Securities Act 1981 (Vic) was designed to address the special problem of inequity that can arise where a vendor purports to pass ownership in goods to a purchaser, when he does not enjoy the title to do so. By adopting a system of registration of interests, the Act seeks to address an application of an understandable principle of the law which, in individual cases, can be unfair and unreasonable.

The third agency of change, supporting the second, is the law reform institution itself. Scattered throughout this book are references to reports of the Law Commissions of England and Wales and of Scotland, of the Ontario Law Reform Commission and of the New South Wales Law Reform Commission and South Australian Law Reform Committee. As well, the law reforming effort of Professor Peden's inquiry and the Swanson Committee are also mentioned.

The Australian Law Reform Commission has examined this area of the law only in the context of insurance contracts — that being a Federal area of legal responsibility and one referred to the Commission by the Attorney-General.[18] The resulting proposals have taken most of the approaches that it is open to the law to take in response to unacceptable contractual terms:

- In some cases unacceptable terms are specifically excluded (as for example 'other insurance' provisions).
- In other cases uniform terms and conditions are to be defined by law (as in 'standard cover' for the main areas of domestic insurance).
- Additionally, in respect of terms inconsistent with 'standard cover' provisions, these will only operate against the insured to the extent to which they provide cover which is not less than the standard or they have been drawn to the insured's specific attention.

. Finally, in some cases a discretion is conferred upon the court to adjust the interests of the contracting parties equitably (as for example in certain cases of fraudulent non-disclosure or misrepresentation where the loss of cover would be seriously disproportionate to the harm caused).

Legislation based upon this report is before the Australian Federal Parliament at the time of writing.[19] Although, if enacted, this Federal legislation will contribute to the miscellany of statutory rules controlling exclusion and like clauses, it will necessarily be limited to contracts of insurance. It will exclude State insurance. A larger measure dealing with contracts more generally remains for the future.

Unhappily, the general Australian law of contract has not been examined by any Australian law reform agency in a comprehensive way. The need for such an examination was outlined nearly a decade ago by Professor JG Starke in an important essay in the Australian Law Journal.[20] In an editorial in the journal, Professor Starke called attention to the success of United States efforts in the restatement of the law of contract. The American Law Institute's restatement has been profoundly influential in the United States. The differences between law reform and research directed 'not towards reform but towards clarification or systematisation of the law' were specifically mentioned.[21] Yet nearly a decade later, we are still waiting for the beginning of a coherent approach to contract law reform. This book gives further illustration of the need to bring order, concept and principle into what is, at the moment, an 'unmanageably complex' area of the law — and one growing ever more complex with reforming legislation enacted in differing terms in different Australian States, applying to parties differently defined and providing different relief.

As Australia moves towards computerisation of commercial transactions and contracts negotiated and effected by trans border data flows, the needs for more uniform, simple and commercially realistic rules will become more manifest.

This book

This book will contribute to Australian reform in a number of ways. First, the author has been at pains to draw to attention the numerous proposals for law reform emanating from law reforming agencies.

Secondly, a book amply demonstrates the conclusion announced in the final chapter. Even if we confine ourselves to recent common law and legislative developments, this is clearly an area of the law in need of clarification, simplification and restatement, if not reform. The common law has taken its meandering course backwards and forwards over the hill of 'fundamental breach'. The law reformers have dealt with bits and pieces. Especially in Australia, the legislation has come in confusing variety. The interaction between Federal and State legislation is, to put it mildly, unclear. Diversity, which is such a notable and valuable feature of the Federal system of government, may not be specially useful in the area of business law. Such use as it had in earlier times may melt before the sun of informatics, if it has not already disappeared in consequence of the high level of integration already achieved in the Australian economy.

A third contribution to reform will be the valuable insights offered by the author to novel lines of inquiry. Reference to the national and economic background against which a modern law of contract must be developed occurred in the judgments of Justices Stephen and Murphy in Port Jackson Stevedoring Pty Limited v Salmond & Spraggon (Australia) Pty Limited.[22] Each of these High Court Justices appeared to be of the opinion that Australian courts should not necessarily agree to a doctrine on exemptions from liability which, as the author puts it, 'assisted ship-owning nations to the detriment of ship-user nations' — Australia being one of the latter.[23] In the past, it has simply been assumed that the common law of contract, largely developed in the busy circumstances of 19th century trading Britain, was appropriate and just for the very different economic circumstances of Australia. Only lately has legislation begun to explore the legitimate economic and social differences.

The other hint of methodology is found in the interesting section of this book which explains a Tasmanian survey which was designed to discover the actual attitudes of businessmen to a series of differential questions relating to the operation of exclusion clauses. Such an empirical approach, rather than assumptions about the operation of the law, is surely the way in which reform or renewal of the law of contract in the future should be addressed.

The lesson of this book may be that we are not moving from principles to pragmatism, nor even from principles to principles. The lesson may be that we are stumbling in our courts, our Parliaments and law reforming agencies from one set of pragmatic rules to another — aiming to effect commercially realistic but fair adjustments between contracting parties, in their infinite variety. Almost certainly, a simpler, more coherent and more effective body of law could be developed if only we were to identify more precisely the competing social and economic policies that the law is struggling here to uphold.

In default of such an effort, Australia will doubtless continue to move from one minor reforming adjustment to another. The task of conceptual re-examination will remain for some Luther of contract jurisprudence in the future.

Sydney
2 April 1984

M D Kirby

FOOTNOTES

1. Citing Yates, Exclusion Clauses in Contracts, 264. See chapter 9.

2. Suisse Atlantique Societe d'Armement Maritime SA v MV Rotherdamsche Kolen Centrale [1967] 1 AC 361; [1966] 2 All ER 61.

3. TNT (Melb) Pty Limited v May & Baker (Aust) Pty Limited (1966) 115 CLR 353; (1966) 40 ALJR 189.

4. Photo Production Limited v Securicor Transport Limited [1980] AC 827; [1980] 1 All ER 556. See discussion in chapter 1.

5. Karsales (Harrow) Ltd v Wallis [1956] 1 WLR 939; Harbutt's Plasticine Limited v Wayne Tank & Pump Co Limited [1970] 1 QB 447; [1970] 1 All ER 225.

6. See J Atkin, 'Fundamental Breach and the Nature of Exclusion Clauses' (1981) 9 Syd L Rev 434; M Hetherington, 'Contracting OUt of Discharge for Breach' (1980) 3 NSWLR 233.

7. PS Atiyah, The Rise and Fall of Freedom of Contract, 1979.

8. PS Atiyah, 'Contracts, Promises and the Law of Obligations' (1978) 94 LQR 193.

9. ibid; 209.

10. PS Atiyah, 'From Principles to Pragmatism : Changes in the Function of the Judicial Process and the Law'. Inaugural Lecture, 1978, Clarendon Press, Oxford.

11. J Stone, 'From Principles to Principles' (1981) 97 LQR 224.

12. O Kahn-Freund, Book Review (1980) 15 JSPTL 81.

13. Cf Murphy J in Port Jackson Stevedoring Pty Limited v Salmond & Spraggon (Australia) Pty Limited (1978) 139 CLR 231; (1978) 18 ALR 333, 376. Note that the decision was reversed by the Judicial Committee of the Privy Council. See chapter 6.

14. The position of insurance was referred to by Kerr LJ in George Mitchell (Chesterhall) Limited v Finney Lock Seeds Limited [1983] QB 284; [1982] 3 WLR 1036, 1056, 1057. See chapter 4 ('The insurance factor').

15. Menzies J in South Australian Railways Commissioner v Egan (1973) 130 CLR 506; (1973) 47 ALJR 140, 141.

16. See for example the decision in Lloyds Bank Limited v Bundy [1974] 3 WLR 501. Discussed in chapter 4.

17. J Peden, Report on Harsh and Unconscionable Practices, 1976, discussed chapter 4.

18. Australian Law Reform Commission, Insurance Contracts (ALRC 20), 1982.

19. Insurance Contracts Bill 1983 (Cth).

20. JG Starke, 'A Restatement of the Australian Law of Contract as a First Step Towards an Australian Uniform Contract Code' (1975) 49 ALJ 234.

21. (1975) 49 ALJ 209.

22. (1978) 139 CLR 231; (1978) 18 ALR 333.

23. ibid, Stephen J, 258-9; Murphy J, 284-5.