THE PROBLEM OF EXCEPTION CLAUSES : A THEORY OF PERFORMANCE-RELATED RISKS

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Introduction

The treatment of exception clauses is one of the most discussed subjects in Anglo-Australian contract law and continues to pose perplexing problems. The House of Lords in *Photo Production* v. *Securicor Transport* made some significant pronouncements on freedom of contract but failed to provide future courts with any more certain guidance to the problem of excessive exception clauses.[1] The controversy over the 'construction' of exception clauses and their 'juristic function' promises to continue (albeit on a different plane in the light of a more liberal view of freedom of contract).

It is submitted that we have not really come to grips with the crucial problem of exception clauses, namely, when is a performer under a contract liable for his own misperformance notwithstanding the presence of an exception clause *prima facie* exempting him from liability?

The purpose of this article is therefore to address this problem of exception clauses and show how in England and Australia, exception clauses can be sensibly and effectively controlled by a means already available in the common law. For in the cases, most of which involve the 'defunct' doctrine of fundamental breach, the courts have intuitively marked out various types of misperformance, mainly those within the control of the performer, for which liability cannot be excused by the incorporation of an exception clause. In other words even an exception clause does not always imply that a party has necessarily accepted all the risks of a contract, including those of misperformance which the clause attempts to cover. Fuller analysis of the cases shows a differentiated scale of misperformance against which a performer cannot protect himself if they are avoidable or culpable. These indicia of culpability bear only a vague resemblance to notions of moral reprehension or fault in tort law and form a basis for a theory of what will be called risks of avoidable misperformance, or more briefly, 'performance-related' risks.

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1. See e.g. Ogilvie, 'The Reception of Photo Production Ltd. v. Securicor Transport Ltd. in Canada: Nec Tamen Consumebatur' (1982) 27 *McGill L J.* 424.

Before sketching out the theory of performance-related risks, it is proposed to bring the crucial problem of exception clauses into sharper focus. To do so, we shall study a theme of conflict between a 'strict principle' and an 'adjustment principle' that underlies contract law and which defines the problem in a historical perspective. It is also necessary to reconsider in this article Professor Coote's theory of the juristic function of exception clauses. The theory that exception clauses define and limit rights and liabilities is not new. Nor is it now open to dispute. But recently, even the efficacy of legislative responses to exception clauses has been seriously doubted because they have allegedly failed to take into account the juristic function of exception clauses.[2] Thus any attempt to offer a means of dealing with exception clauses must confront Coote's theory. Part II accordingly shows more precisely the role of the juristic function. It will be argued that the importance of the juristic function has been overrated and that at the same time the context in which it has relevance has been inadequately considered.

In the pages that follow, legal history is combined with interpretative analysis to develop the theory of performance-related risks. It has often been necessary to refer to the detailed factual patterns of cases because the familiar elusive linguistic quality of the common law masks significant shifts in the case law. It is not the aim to consider in detail fine factual differences that determine the outcome of marginal cases but to develop a theory which will determine the legal margins of control of exception clauses.

A Theme of Conflict

In Anglo-Australian contract law, early notions of a severe breach developed independently of exception clauses. They were concerned with when a party might terminate or repudiate a contract, the general principle being that one cannot terminate or repudiate a contract except where there is either an express provision to this effect or the aggrieved party is discharged of his obligations since the other's breach of contract 'goes to the root of the contract', or amounts to the breach of an 'essential obligation' or of a 'condition' rather than a 'warranty'. Generally a breach was 'severe' if it resulted in the collapse of a bargain.

At first the aggrieved party was regarded as having assumed all risks unless otherwise specified. Courts kept strictly to the letter of the contract; they took their role to be that of upholding the express contract with total respect for the sanctity of terms. So in the old case of *Chandelor*

2. E.g. Palmer and Yates, 'The Future of the Unfair Contract Terms Act 1977' [1981] *Camb L.J.* 1080; Coote, 'Unfair Contract Terms Act 1977' (1978) 41 *Modern L.Rev.* 312.

v. *Lopus*,[3] caveat emptor was held to apply rigidly; the seller not having warranted his horse to be "good", there "is no cause of action". Similarly in *Paradine* v. *Jane*[4] the parties were left to anticipate and provide for the consequences of every contingency; otherwise they were bound according to the express terms of the contract, the court refusing to fill any gaps. It followed that unforeseen circumstances including *force majeure* which rendered a performance either substantially wanting to the buyer, or impossible, or highly onerous to the performer could not give a right to repudiate.

It was not appreciated that in the time lapse between the formation and the performance of a contract innumerable new circumstances can arise which the parties cannot really anticipate but which may seriously affect the pattern and extent of risks assumed by each party in the contractual relationship. Nor was it seen that while the parties could make a sufficiently 'certain' contract for the purposes of 'forming' or 'making' a bargain, so as to create a 'binding' bilateral relationship between them (if only to cut off the offeror's right to revoke his offer or promise), this did not suffice to answer the question of *what performance* was due from the promisor in the circumstances. To cope with these problems raised by the bilateral contract, the courts needed new devices to adapt a contract in the light of supervening realities. As Street has observed, the bilateral contract is "based solely upon consent" only in the sense that its obligatory force is contractual and is not founded on any other legal duty.[5]

One such regulatory device came with the introduction of the implied term. By means of an implied term, courts could write into a contract terms which the parties had not agreed on and so adjust their exchange positions. As Lord Ellenborough said in *Gardiner* v. *Gray*,[6] a landmark case, a purchaser cannot be supposed to buy goods to lay them on a dunghill. In other words, in spite of the sanctity of terms, the courts now began to recognise that an exchange by bargain could not or should not result in a total failure of consideration: that (putting this a little differently) the buyer must get something for his money.

Another (and for present purposes more important) regulatory device began with the seminal decision in *Boone* v. *Eyre*.[7] Here a buyer was held not entitled to refuse payment of the price for a plantation with a stock

3. (1603) Cro.Jac. 4, 79 E.R. 3.
4. (1647) Aleyn 26, 82 E.R. 897; Connor v. Spence, (1878) 4 V.L.R 243 at 259.
5. As were for example, the early real contract or simple debt before it. *The Foundations of Legal Liability* Vol II,(1966) chap.I-VI.
6. (1815) 4 Camp. 144, at 145, 171 E.R. 46 at 47.
7. (1779) 1 H.Bl. 273n., 2 W.Bl. 1312n., 126 E.R. 160n.

of negroes even though the seller had not fully complied with the express terms of the sale. The latter had already conveyed the estate but could not, contrary to his covenant, make complete title to all the negroes. The covenant was said to be one of minor importance. It went only to 'part' of the consideration: the buyer had received title to all but a few negroes. The misperformance did not disable the seller from his action. For "[if] this plea were to be allowed, any one negro not being the property of the plaintiff would bar the action".[8]

Quite clearly, the court was striving for a reason to disallow the aggrieved buyer the benefit of default by the seller in this partly executed covenant.[9] The covenants, said the court, "are executed in part, and the defendant ought not to keep the estate because the plaintiff has not a title to a few negroes".[10] There was evidently no relation between the importance of the stipulation broken and the amount of benefit a party might have obtained up to the time of the breach. *Boone* v. *Eyre* was primarily concerned with the question of whether a buyer had to pay for a performance even if incomplete. But although the distinction between the whole and part of the consideration in *Boone* v. *Eyre* provided a flexible calculus as to when a buyer was entitled to refuse to perform his own contractual obligations it was not clear how great or small a 'part' had to be.[11]

In *Boone* v. *Eyre* itself the seller's lack of title in the few negroes could be said without particular difficulty to be only a 'part' of the consideration. If the breach might be adequately compensated by damages, Lord Mansfield had suggested, the breach did not go to the "whole of the consideration", hence the buyer could not repudiate, damages being adequate as a remedy. It was henceforth clear that some contractual terms might require less fulfilment than others and might be adjusted. The gravity of the breach relative to the part performed determined the buyer's right to refuse to perform; or, as it came to be generally said, if the seller had performed a "substantial part of the contract" the buyer could only recover damages.[12]

8. Id per Lord Mansfield
9. "[I]f, in the case of Boone v. Eyre, two or three negroes had been accepted, and the equity of redemption not conveyed, we do not apprehend that the plaintiff could have recovered, the whole stipulated price, and left the defendant to recover damages for the non-conveyance of it", per Pollock C.B. in Ellen v. Topp (1851) 6 Exch. 424 at 442, 155 E.R. 609 at 616.
10. Per Ashurst J. whose judgment is not reported but can be gleaned from Campbell v. Jones (1796) 6 T.R. 570, 101 E.R. 708 at 710.
11. In Bastin v. Bidwell (1880-81) 18 C.D. 238, Kay J. thought it was "not a very fortunate use of language to say 'where covenants go to the whole consideration on both sides', but the meaning is very clear "
12 Ellen v. Topp supra n.9 in per Pollock C.B. In Forman v. The Ship "Liddesdale" [1900] A.C. 190, it was said that there must be no material difference in kind between the work, so far as it was executed, and the work contracted for.

Furthermore, the fact that *Boone* v. *Eyre* was a case involving an executed covenant and not an executory simple contract was overlooked, and the part-whole distinction was extended to executory simple contracts. The result was that after *Boone* v. *Eyre* an averment of performance was needed only where the mutual stipulations went to the "whole of the consideration"; or, putting this in less procedural language, only where the promisor's breach was fundamental did the other party have the right to repudiate. So in *The Duke of St. Alban's* v. *Shore*,[13] the buyer could repudiate an agreement to convey land when the seller cut timber on the land before the completion of the conveyance, thereby diminishing the value of the land considerably. What the seller did went not just to a 'part' but to the 'whole' of the consideration, and the buyer was not obliged to pay for an estate which was substantially different from that under the contract.

What went to the 'root' or 'whole' of the consideration differed between executory and executed contracts. In the former the criterion as applied was more rigid, unless there were special situations such as instalment contracts, or special service contracts such as those in *Bettini* v. *Gye*[14] and *Poussard* v. *Spiers*.[15] In *Bettini* v. *Gye* it seemed to have been material in Blackburn J.'s opinion that although the impresario may not as yet have benefitted from the agreement, the late start did not prejudice him either. On the other hand, in reliance on the agreement the singer had incurred detriment by foregoing any possible alternative employment for its duration. Consequently the impresario could not refuse the services of the singer. In *Poussard* v. *Spiers* a prima donna was to perform in a new opera for three months. After attending several rehearsals as expected, she fell ill and could not attend the last few rehearsals. The impresario, being uncertain how long her illness might continue, provisionally engaged a substitute who was to receive a douceur if she was not needed. Otherwise she was to be permanently employed for a weekly salary till 25 December. The prima donna continued to be too sick to attend the opening performance and the following three performances. On 4 December she tendered her service which was refused. It was held that the impresario could not be expected to adopt a "ruinous" course as would have been the case if he had to postpone performances for the uncertain duration of the prima donna's serious illness. Nor could he be expected to incur

13. (1789) 1 H.Bl. 270, 126 E R. 158 Even when it was recognised in Graves v. Legg (1857) 2 H. & N. 211, 157 E.R. 88 that Boone v Eyre related to an executed convenant and not an executory contract, it was not fully appreciated that Boone v. Eyre was mainly concerned with whether a buyer had to pay for a performance rendered even if incomplete, whereas in executory contracts the question was whether a buyer could reject any performance tendered.
14. (1876) 1 Q.B.D. 183.
15. (1876) 1 Q.B.D. 410.

substantial detriment by retaining her services and at the same time employing a substitute by permanent engagement.

The practical considerations underlying the decisions in the two cases have been overshadowed by the attention paid to Blackburn J.'s test, invoked in both cases, of whether the term "[went] to the root of the matter", so that a failure to perform it would render performance of the rest of the contract a thing "different in substance" from that which the aggrieved party had stipulated for. It was subsequently observed that "like most metaphors, [Blackburn J.'s test] is not nearly so clear as it seems".[16]

Concern that the seller should not incur disproportionate loss where he had invested for future performance is well exemplified in the various decisions relating to instalment contracts. In a sale of 667 tons of iron to be shipped in four monthly shipments, which were to be "about equal" it was held that a shipment of twenty one tons at the outset could be rejected by the buyer who could also refuse to accept the rest.[17] But an unsatisfactory delivery in the course of the contract would not entitle the buyer to similar remedies,[18] as where a single delivery of one and a half tons of seriously defective flock in a sale of 100 tons did not entitle the buyer to refuse to accept delivery.[19]

In the interest of the buyer who had paid and received none of the agreed benefit under a contract, the doctrine of total failure of consideration was developed to give him a quasi-contractual remedy of recovery. Unlike *Boone* v. *Eyre* which protected to some extent the seller who had invested in the performance of the contract, total failure of consideration rather protected the buyer who was allowed to repudiate and to recover his money despite any expenses that might have been incurred by the seller in the purported execution of the contract. This was true even though in most cases the seller's expenses were insignificant.

At first a buyer had a remedy in money had and received only upon the non-delivery of the consideration. If, however, the goods delivered were so different in kind that they were not to be regarded as a delivery at all, or if they were worthless, a buyer who had paid in advance was allowed to repudiate and to recover the price paid. An action in indebitatus, it was said, was possible if, to use the well known examples,

16. In Bank Line v Capel [1919] A C. 435 (H.L) at 459 per Lord Sumner The same test was nevertheless applied by Australian courts in Fuller's Theatres v Musgrove (1923) 31 C.L R 524 at 537-8, and Attorney-General v Australian Iron and Steel (1936) 36 S R (N S.W) 172 at 180-1; and cited in Associated Newspapers v Bancks (1951) 83 C.L R 332 at 337.
17. Hoare v Rennie (1859) 5 H & N 19, 157 E.R. 1083.
18. Jonassohn v Young (1863) 4 B & S. 296, 122 E.R 470
19. Maple Flock v Universal Furniture Products (Wembley), [1934] 1 K B 148 at 157 The gravity or significance of the breach was said to depend on the ratio quantitatively which the breach bore to the contract as a whole and the degree of probability and improbability that such a breach would be repeated.

sawdust instead of fish was delivered in a contract for fish,[20] or if counters were delivered in a sale of foreign gold coins,[21] or if a bar was sold as gold but was in fact brass.[22] In these examples, the courts would permit recovery in the absence of fraud or of any express warranty, and not because of any implied warranty (which was not fully recognised yet). The 'total' failure was not a literal one.[23] For instance, a buyer who had paid money in excess could recover the excess when there was not a complete failure of consideration.[24]

With these new devices protecting sellers and buyers according to whether the contract was executed or executory, the development of the law followed a course involving the struggle between two opposing ideas — the sanctity of terms on which the strict approach is based, and the adjustment of the exchange relationship of the parties in the event of supervening events including a party's breach, subsequent to the formation of the contract. The notions of severe breach embodied the compromises struck between these two ideas; the compromises varying generally with the degree of performance rendered and conversely with the consequences of the breach. These compromises manifested themselves differently in different types of transactions, but they were based on a common conception of the bilateral contract as an exchange by bargain.

Not that this struggle had uniform results. The theme of conflict and compromise that emerged was at the same time countered by the adoption of the strict approach in many cases, a telling example of which was *Bowes* v. *Shand*.[25] A majority of the House of Lords in that case adopted the strict approach; according to the minority this disregarded the seller's performance and disproportionate loss. The strict approach was also bolstered by the consensus theory of bilateral contracts which amplified the element of 'intention' to the extent of obscuring a key distinction between the issues of the formation of a bilateral contract and its performance. The truth is that 'consent' gave the bilateral contract legal validity but there was no logical necessity for it to reign supreme in the arena of performance.

20 Fortune v Lingham (1810) 2 Camp 416, 170 E R 1202.
21. Young v. Cole (1837) 3 Bing (N C.) 724 at 730, 132 E R. 589 at 592
22 Gompertz v. Bartlett (1853) 2 El & Bl 849 at 854, 118 E.R 985; see also Cox v Prentice (1815) 3 M. & S 344, 105 E R 641; cf Devaux v Conolly (1849) 8 C B. 640, 137 E R 658; Jones v.Ryde (1814) 5 Taunt 488, 128 E.R 779, Stoljar, 'The Doctrine of Failure of Consideration' (1959) 75 *L Q Rev* 53.
23 Hunt v. Silk (1804) 5 East 449, 102 E.R. 1142 applied the total-partial distinction literally, see generally 9 *Halsbury's Laws of England*, 4th ed. (1954) para 670.
24 Cox v. Prentice (1815) 3 M & S 344, 105 E.R. 641.
25. (1876) 1 A.B D. 470, (1877) 2 Q.B.D 112, (1877) 2 App.Cas. 455. Morison notes an "unusual divergence of judicial opinion" on this question in executory contracts, *Rescission of Contracts* (1916) at 73.

When courts responded to the need for remedial adjustment of the exchange positions of the parties, their true concerns were often either not wholly conscious or acknowledged, or were deliberately disguised to avoid offending the concepts of sanctity of terms and freedom of contract. These concepts in turn resisted the adjustment principle which was seen as the epitome of judicial interference and the antinomy of established law.

Had it not been for the gradual shifts in its meaning, the concept of freedom of contract need not be opposed to the adjustment principle. Freedom of contract was originally to ensure freedom of action and not to enshrine the idea that bargains are unalterable.[26] It had an eminently practical purpose. When the awkward and limited typical contracts in the fifteenth and sixteenth centuries outlived their usefulness, some means of facilitating the ever-increasing types of transactions were necessary. Freedom of contract, encompassing the notion of consensus, provided an elastic instrument for the infinite varieties of dealings by reducing the "ceremony necessary to vouch for the deliberate nature of a transaction" to a minimum.[27] But under the influence of laissez faire ideals it became a manifestation of free trade. Relations between men, it was also asserted, ought to rest on mutual free consent and not on coercion on the part of the state and society.[28]

The concordance of two sets of external signs manifesting the intention of the parties became central to the notion of contract, but with a difference. The importance of this idea was shifted from its central significance as the basis of the legal validity of the bilateral contract to the redefined judicial role of strict adherence to the letter of the contract. As a result contract became a private matter between the parties in which, it seemed to follow, the courts could only provide for the interpretation

26 Angelo and Ellinger explain that a study of the relevant provisions in the Prussian Code (para. 1 3 1), the Code Civil (1108-1122) and the German Code (116 and 145) shows that freedom of contract was originally and primarily to ensure freedom of action and not to consecrate bargains 'Unconscionable Contracts — A Comparative Study' (unpublished manuscript contributed to the Canberra Law Workshop II (28-29 October 1977) 1-50); Wilson, 'Freedom of Contract and Adhesion Contracts' (1965) 14 *Int Comp L Q* 173 German jurisprudence recognises that freedom of contract means: the freedom to enter into a transaction (the Abschlussfreiheit) and the freedom to codetermine the terms (the Gestaltungsfreiheit).

27 Kessler, 'Contracts of Adhesion — Some Thoughts about Freedom of Contract' (1943) 43 *Columbia L Rev* 629; for a fuller exposition, see Street, supra n 5, chaps I-IV; see also Wilson, 'Freedom of Contract and Adhesion Contracts' (1965) 14 *Int Comp L Q* 172, Kessler and Gilmore, *Contracts Cases and Materials*, 2nd ed (1970) 36-37, Williston, "Freedom of Contract" (1921) 6 *Cornell L Q* 365

28 Adam Smith's economic laissez faire, e.g , postulated that if individuals were allowed to pursue their self-interest free from governmental interference they would maximise their own profits and thus the wealth of the society as a whole. Competition of individual self-interests would result in social harmony through the agency of the "invisible hand" and contract was to be instrumental Similarly, Bentham, James Mill and J.S Mill preached the absence of restraint. See Pound, 'Liberty of Contract' (1908) 18 *Yale L J* 454, "unlimited freedom of making promises was a natural right . .."; Viner, 'The Intellectual History of Laissez Faire' (1960) 3 *L J & Econ* 45 at 59-61; P.S. Atiyah, *The Rise and Fall of Freedom of Contract* (1979)

of contracts and could not 'rewrite' them or impose their views on the parties. Once there was a manifestation of assent the parties were bound according to the contractual rights and duties specified in the contract whatever might subsequently happen to make nonsense of them. Freedom of contract thus became the "inevitable counterpart of a free enterprise system" in a form quite different from its original. The judicial attitude towards freedom of contract was, for a long time, epitomised by Sir G. Jessel F.M.'s much quoted statement that:

> if there is one thing more than another which public policy requires, it is that men of full age and competent understanding shall have the utmost liberty of contracting and that their contracts, when entered into freely and voluntarily, shall be held sacred and shall be enforced by courts of justice.[29]

Frustration of the Venture

If contracts were to be held sacred, what were the legal consequences on the contractual relationship between parties where a performer, because of an unforeseen and unavoidable supervening contingency, could not perform his obligations due under the contract? Where there was a clear case of physical impossibility, he was excused by law.[30] The more common problem, especially in charterparties, however, involved a temporary impossibility brought about by a *force majeure*. A shipowner was protected from liability for failure to perform duly only if he had secured for himself an express excuse under the contract, for instance, by including the usual 'exception of perils' clause. His obligations were suspended by virtue of the express exception clause for the duration of the temporary impossibility and he was excused from performing duly. That being all the protection expressly provided for, he could not repudiate the contract. It followed that the charterer could not repudiate either. Both were bound in the absence of express provision to the contrary until such time as the temporary impossibility was over and one party breached the contract by not performing. The parties, it was said in *Hadley* v. *Clarke*,[31] "must submit to whatever inconvenience may arise therefrom unless they have provided against it by the terms of their contract".

29 Printing and Numerical Registering v. Sampson (1875) L R 19 Eq 462 at 465; Mogul Steamship v McGregor [1892] A.C 25, A G of Commonwealth of Australia v. Adelaide Steamship [1913] A.C 781

30 See e.g. Hyde v. Windsor (1657) Cro Eliz 457, 78 E.R. 710 (death), Hall v. Wright (1859) El.B. & El 746, 120 E.R 688 (sickness which disables performance)

31. (1799) 8 T.R. 259 This case was later disposed of by Metropolitan Water Board v Dick, Kerr [1913] A C 119 (H L) at 127 per Lord Finlay, L C.

The contract still subsisting, both shipowner and charterer had to perform according to the provisions of the contract once the temporary impossibility was over. Thus a charterer still had to load under a contract for the shipment of fruits after the removal of an embargo even though the season for shipping had long since passed and the voyage was rendered useless to him.[32] The shortcomings of such an approach were evident. In no sense could it be said that the purpose of a charterer, who quite clearly needed his fruits to be shipped for a certain market, was to have the service of a shipowner's carrier at a time when there was perhaps neither fruits to ship nor the market for them. By holding him to an arrangement which in changed circumstances was completely different amounted to making him assume all risks of supervening events.

It was gradually recognised that contracts were not agreements to do something simpliciter but were more realistically ventures in respect of which certain types of risks were not within the 'realm of the bargain'. Protection was thus extended to the charterer on the ground of (what was now called) frustration of the venture. An early application of the idea occured in *Freeman* v. *Taylor*[33] where it was said that if the delay was "so long and unreasonable that, in the ordinary course of mercantile concerns it might be said to have put an end to the whole object [of] the freighter" the charterer could be excused. In that case the shipowner's deviation and resulting delay of six weeks was found to have deprived the charterer of the benefit of the contract and excused his refusal to load as he was obliged to do under the contract. This was a departure from a relic of the rules of independency and dependency which said that an undertaking to arrive for loading at all speed, as was the case here, was independent and would allow a shipowner to bring an action on the contract. In *Tarrabochia* v. *Hickie*[34] the jury was directed to decide if the "object of the charter-party and of the voyage therein mentioned was wholly frustrated by the delay or the alleged unfit condition of the ship". Only a delay or deviation which "entirely frustrates the object of the charterer in chartering the ship" could excuse his non-performance.[35]

The ideas germane to *Freeman* v. *Taylor* and *Tarrabochia* v. *Hickie* were quite clearly concerned with a different and more difficult problem than

32 Touteng v. Hubbard (1802) 3 B & P 291, 127 E R 161 The case was decided in the charterer's favour on the ground that a Swedish subject could not recover from a British subject damages incurred as a result of reprisals taken by the British government against the Swedish government. But Lord Alvantely C.J. would clearly not have resolved the problem in different circumstances other than by a strict approach. Hadley v Clarke, he said, would apply (at 165).

33. (1831) 8 Bing. 125, 131 E R 348.

34. (1856) 1 H. & N. 183, 156 E.R. 1168

35. MacAndrew v Chapple (1866) L.R. 1 C.P. 643 at 648 "From the time of Boone v. Eyre, Ritchie v. Atkinson, and Davidson v. Gwyne, this rule has been applied".

that encountered in *Boone* v. *Eyre*. In the cases of temporary impossibility the issue was not how great or small a part of the contract has been performed but whether the inordinate delay was such as to defeat the charterer's object in entering into the contract. Complicating the issue was the fact that in the majority of these cases the shipowner was protected by an express provision from an otherwise actionable breach when he failed to perform duly. Would such a clause affect any right of the charterer to be discharged of his obligations?

It became clear in *Jackson* v. *The Union Marine Insurance*[36] that the notion of the frustration of the venture applied equally to collapses of bargains resulting from a performer's actionable breach as well as from his excusable failure to perform. In *Jackson's Case*, the shipowner was to proceed "with all possible dispatch" to Newport to load a cargo of rails for San Francisco, "dangers and accidents of navigation excepted". The ship was grounded by perils of the sea, a cause within the exception clause, and was damaged with the result that the voyage would have taken eight months longer than the normal time. In the meantime the charterer had abandoned the charter. According to the literal interpretation of the contract, the ship would have arrived in time. Nevertheless, it was held that the delay was so material to the charterer who needed the rails for a railway that he was excused from his performance of the contract after the ship was grounded for six weeks. As the charter was for a definite voyage "there is *necessarily* an implied condition that the ship shall arrive at Newport in time for it".[37]

The court rejected the shipowner's argument that regardless of whatever contingencies that may arise subsequent to the formation of the contract, he, the shipowner, was still bound to take and had the right to demand the cargo of the shippers.[38] Whether the delay was caused by the shipowner's default or by *force majeure*, the charterer could still be discharged after the lapse of a reasonable time. The charterer's right of discharge was independent of any express or implied exception clause. The exception clause was an excuse for the shipowner who was to perform, and saved him from an action. It made his non-performance not a breach of contract, but did not operate to take away the right that the charterer would have had, if the non-performance had been a breach of contract,

36. (1874) L R. 10 C.P. 125.
37. Italics in the original; Id. at 142-3. The majority relied strongly on Freeman v. Taylor, Tarrabochia v. Hickie, and MacAndrew v. Chapple
38. (1874) L.R. 10 C.P. 125 at 142.

to "retire from the engagement".[39] The charterer's remedy is now known to be for a failure of consideration in the executory sense. This was confirmed two years later in *Poussard* v. *Spiers* by Blackburn J. who was also a member of the Court of Exchequer Chamber in *Jackson's Case*. He pointed out the "complete analogy" between the two cases, in each of which was such a "failure of consideration" that the aggrieved party was entitled to rescind.[40]

Since the charterer's right was an option to repudiate the contract when inordinate delay resulted from a *force majeure* it followed that he could consider himself still bound to the contract and hold the shipowner to his side of the bargain. But in *Geipel* v. *Smith*[41] the modern doctrine of frustration had begun: the shipowner was discharged of his obligations under the contract where its object was frustrated. On facts similar to *Hadley* v. *Clarke*, the court in *Geipel* v. *Smith* held that the shipowner was discharged of his obligations under the contract when the object of completing the contract within a reasonable time became impossible. The contract, Blackburn J. explained, was not for a voyage at some indefinite time in the future but contemplated a "commercial speculation within a reasonable time"[42] and a blockade was a "restraint of princes"[43] which was "likely to continue so long and so to disturb the commerce of merchants, as to defeat and destroy the object of a commercial adventure like this".[44] The presence of the express exception of 'restraint of princes' suggested that the delay was a "possibility within the contemplation of the contract".[45] And because the performer's commercial object of the venture was defeated he was entitled not only to a suspension of his obligations but also to have them discharged. To otherwise hold him to the contract promoted deplorable economic waste.

But the notion of the frustration of the venture became obscured mainly as a result of two complications, neither of which had anything to do with its basic thrust, which was to protect the charterer. One was the applica-

39 Id., at 145: "[T]here are the cases" said Baron Bramwell, "which hold that, where the shipowner has not merely broken his contract, but so broken it that the condition precedent is not performed, the charterer is discharged . Why? Not merely because the contract is broken If it is not condition precedent, what matters it whether it is unperformed with or without excuse? Not arriving with due diligence, or at a day named, is the subject of a cross-action only. But, not arriving in time for the voyage contemplated, but at such a time that it is frustrated, is not only a breach of contract, but discharges the charterer. And so it should, though he has such an excuse that no action lies" (at 147).

40 (1876) 1 Q B.D 410 at 414

41 (1872) L R 7 Q B. 404; per Lord Sumner in Bank Line v Capel [1919] A C 435 (H L) at 455 See generally R G. McElroy and G L Williams, *Impossibility of Performance* (1941) 77 ff , 123 ff

42 (1872) L R 7 Q B. 404 at 413

43 Id at 412

44 Id. at 414-5 per Lush J

45 Per Lord Watson in Dahl v Nelson (1880) 6 App.Cas 38 at 59

tion of frustration of the venture for the protection of the shipowner. The significance of *Geipel* v. *Smith* was not as yet fully appreciated. In *Jackson's case* itself, it was thought that the shipowner and the charterer not being at fault, both were released from the contract: "if one party may [rescind], so may the other".[46]

This line of argument was taken further in *Tamplin Steamship* v. *Anglo-Mexican Petroleum*.[47] In that case, a ship was hired on a time charter for five years for the carriage of oil with the usual form of clause excepting "restraint of princes, rulers and peoples". The ship was requisitioned by the Admiralty and altered making her unsuitable for oil when the charter had almost three more years to run. It seemed at the time of the requisition that it could be for the duration of the war, but in fact it ended before the expiry of the original term. The admiralty paid compensation in excess of the hire. It was assumed that if the contract was avoided the shipowner would be entitled to the compensation. Consequently, the shipowner sought to repudiate the contract while the charterer contended that the contract subsisted and he was ready and willing to perform. A majority of the House of Lords was not prepared to allow the shipowner the substantial benefit which he had not bargained for and held that the contract subsisted.[48] It was clear that had the special facts not been present and had the charterer been sued for the hire instead, the charterer would not have to pay because the venture was frustrated. The dissenting minority, however, held that the contract had fundamentally collapsed: the requisition went to the root of the consideration and "relieve[d] both parties . . . from their engagements".[49] The requisition it was explained, created a condition of things to which the charterparty was inapplicable, hence discharging both parties. Essentially the courts were concerned to adjust the risks of unforeseen and unavoidable supervening contingencies between two innocent parties. These risks are in a sense 'apportioned' between them: the performer can plead in defence the principle of impossibility (more specifically, what is now known as frustra-

46 (1874) L R 10 C.P 125 at 145 *Contra* Cleasby B. supported the earlier cases because they followed a rule that was "certain clear and not influenced by unfair collateral considerations of interest" while the new rule gave "each party the chance of getting out of the charter, according to his interest to do so"

47 [1916] 2 A C 397 (H L).

48 [O]ne view that ran through the opinions of the majority was this No one was hurt by the continuance of the charter, and if the government relinquished the ship there was no reason why the charter should not be effective for the remaining period of its duration, which might be considerable" and that had the facts been different, that is, had the government taken the ship and had said they would pay nothing . and had the owner sued the charterer for the hire during the requisiton the case would have "fallen within the lines of Horlock v Beal", that is to say, the charterer would not have to pay, per Lord Dunedin in Metropolitan Water Board v. Dick, Kerr [1918] A C 119 (H L.) at 129

49 Id at 421

tion), while the payor is protected by the principle of the frustration of the venture. But the courts themselves were not always aware of the implications of these developments. The notion of the frustration of the venture from the charterer's point of view (as a failure of consideration) and from the shipowner's point of view (as a contemplated risk which he was regarded as having assumed but only to an extent short of defeating his commercial object in contracting) became subsumed under a 'new' and independent doctrine where courts looked for the common object of the contract. Such object, when defeated, it was said, ended the contract.[50]

The implication that both shipowner and charterer were discharged by the same principle was of course mistaken. The charterer did not have to pay when he obtained nothing or absurdly little. "It [was] the further performance of the contract by one party which formed the consideration for the payment by the other, which [had] become impossible"[51] and which enabled the charterer to be discharged. This certainly could not be the reason for relieving the shipowner who was protected by the principle in *Geipel* v. *Smith*.

The other complication was the extension in *Taylor* v. *Caldwell*[52] of the older rule of impossibility under which death of the performer excused his failure to perform.[53] *Taylor* v. *Caldwell* protected a performer from risks of destruction of the particular thing he contracted to deliver and excused him from failure to perform. But the reason given for the performer's excuse was explained in terms of an implied provision to the effect that he was not to be liable and that the contract was to terminate. Indisputably this implied term was "a device by which the rules as to absolute contracts are reconciled with a special exception which justice demands".[54] Unfortunately the implied term in *Taylor* v. *Caldwell* became confused with the implied term mentioned in *Jackson's case* which seemed to account for the consequences of the frustration of the venture in the latter. Impossibility of performance in *Taylor* v. *Caldwell*, frustration in

50. E.g the Coronation and War cases; see the discussions of them by Williams, in 'The Coronation Cases, I' (1941) 4 *Modern L.Rev* 241; 'The Coronation Cases, II' (1941) 5 *Modern L.Rev.* 1.
51. Per Swinfen Eady L.J. in Scottish Navigation v Souter [1917] 1 K.B. 222 at 237, and Admiral Shipping v. Weidner, Hopkins [1917] 1 K.B. 222 at 237.
52. (1863) 3 B. & S 826, 122 E.R. 309.
53. Hyde v. Windsor (1597) Cro.Eliz. 457, 78 E.R. 710 (death); Hall v. Wright (1859) El.B. & El. 746, at 765, 120 E.R. 688 (sickness which disables performance)
54. Per Lord Sumner in Hirji Mulji v. Cheong Yue S.S. [1926] A.C. 497 (P.C.) at 510; Scott v. Del Sel [1922] S.C. 592 at 596 per Lord Sands ("a pious fiction"). See also the observations of Isaacs J. in Hirsch v. Zinc Corporation [1917] 24 C.L.R. 34 at 63-5.

Geipel v. *Smith* and frustration of the venture in *Jackson's case* were consequently treated as virtually one principle.[55]

Recent Manifestations of the Adjustment Principle

In its attempt to provide an acceptable solution to excessive exception clauses, the phenomenon of fundamental breach adumbrates the conflict just described. Fundamental breach is, however, completely different from the earlier notions of severe breach. Generally speaking, as Lord Diplock put it succinctly in *Hongkong Fir Shipping* v. *Kawasaki Kisen Kaisha,*[56] the problem in every bilateral contract is "in what event will a party to a contract be relieved of his undertaking to do that which he has agreed to do but has not yet done". The problem which the doctrine of fundamental breach attempts to resolve is, however, more difficult than those for which *Gardiner* v. *Gray* and *Boone* v. *Eyre* were capital decisions. Fundamental breach seeks to determine when an aggrieved party may still have a remedy against a defaulting performer, despite the presence in the contract of an express exception clause which *prima facie* protects the latter from his own avoidable or culpable (in as much as it is within his control) misperformance, for which he is normally liable. Fundamental breach was thus, one may say, developed almost as a device to control excessive exception clauses. The courts examine the duty of performance in view of an exception clause and find in certain circumstances a fundamental breach which overrides the clause.

In this respect, there is some similarity between fundamental breach and the concept of self-induced frustration. In both the duty of performance comes under scrutiny. In the latter, if the risks of unforeseen and unavoidable supervening contingencies are self-induced, that is they are in some way due to a party's own conduct,[57] he cannot regard himself as discharged of his obligations without liability. If his breach is the frustrating event, he is not protected because he is not entitled to take advantage of his own wrong, be it a deliberate choice not to perform or

55 E g. in Tamplin Steamship v. Anglo-Mexican Petroleum [1916] 2 A.C. 397 where all the speeches assumed expressly or implicitly that the principle applied in the cases of frustration was the same principle in Taylor v. Caldwell: Lord Loreburn (at 404) accepted Knell v. Henry and then went on to say "when this question arises in regard to commercial contracts, as happened in Dahl v. Nelson, Geipel v. Smith, and Jackson v The Union Marine Insurance, the principle is the same, and the language used as to 'frustration of the adventure' merely adapts it to the class of cases in hand"; per Lord Parker at 428; per Lord Atkinson at 406-7, 412, McNair, 'Frustration of Contract by War' (1940) 56 *L Q.Rev* 182; but see McElroy and Williams, supra n.41, where failure of consideration (or frustration of the venture) was clearly identified and distinguished from the modern doctrine of frustration and the rule in Taylor v. Caldwell.

56 [1962] 2 Q B D. 26 at 66

57. Per Lord Sumner in Bank Line v. Capel [1919] A.C 435 at 452; or because "he has brought those circumstances [of frustration] about himself", per Lord Sterndale in Mertens v. Home Freeholds [1921] 2 K B. 526 at 536.

to put performance out of his power. He will also not be protected if his conduct is a contributory cause.[58] For he is considered as not having done enough or not having acted with sufficient industry to give the kind of benefit expected under the contract and therefore ought not to be protected despite the *force majeure* involved.

Although the degree of fault necessary to give rise to self-induced frustration is uncertain, it seems that all deliberate and negligent acts whether amounting to breaches of contract or not are sufficient.[59] Thus where a hirer of a trawler (for use with an otter trawl) chose to use the three licences obtained for the other of the five trawlers operated by him with the result that he could not operate the otter trawl with the hired trawler, he was not protected by the principle of frustration. Although the refusal of a fishing licence in respect of a trawler frustrated the object of the charterparty, it was "the act and election of the [charterers] which prevented the [trawler] from being licensed for use with an otter trawl".[60] Hence the charterparty remained alive and the owners were entitled to the hire.

The similarity between fundamental breach and self-induced frustration is, however, a limited one. Their crucial difference lies in the fact that in cases of fundamental breach a performer is expressly excused from liability for his own breach and the thrust of fundamental breach is to make the performer liable notwithstanding such excuse, whereas in the latter, an issue of frustration, it seems, cannot in the first place arise if the parties have made express provision for the unforeseen supervening contingency.[61]

It should also be mentioned that although fundamental breach was developed mainly in cases involving standard form contracts, its opera-

58. See e.g. The Eugenia [1964] 2 Q.B 226, where a charterer who took his ship into prohibited waters could not plead frustration when it was in consequence detained

59 Denmark Productions v Boscobel Productions [1969] 1 Q.B. 699. In Joseph Constantine v. Imperial Smelting Corp. [1942] A.C. 154 at 179 Lord Russell of Killowen said he wished to guard "against the supposition that every destruction of corpus for which a contractor can be said, to some extent or in some sense, to be responsible, necessarily involves that the resultant frustration is self-induced within the meaning of the phrase" Cf per Cullen C J in Cornish v Kanematsu (1913) 13 S.R (N.S W.) 83 at 89.

60 Maritime National Fish v. Ocean Trawlers [1935] A C 524 (P.C.), at 529. The Canadian Court had taken the view that the risk of frustration was taken by the parties as they both knew at the time of contracting that the licence was required. The Privy Council did not dissent from it but decided on the ground stated. Hirji Mulji v. Cheong Yue S.S., [1926] A C 497 (P.C.) at 507 per Lord Sumner, Denmark Productions v Boscobel Productions [1969] 1 Q B 699 at 725, 736

61. E g Joseph Constantine v Imperial Smelting Corp [1942] A.C 154 at 163 per Lord Simon.

tion is independent of the special form of these contracts.[62] The problem which confronts fundamental breach arises from the use of overwide exception clauses which happen to be common in standard form contracts. Judges and lawyers have often overlooked the fact that it is one thing to use standard form contracts and another to use overwide exception clauses. Consequently they have tended to associate fundamental breach with standard form contracts and to regard fundamental breach as a response to a problem peculiar to such contracts. In this view, fundamental breach could only be developed at the expense of underrating the role of standard form contracts in an economy that supports mass production.

If the phenomenon of fundamental breach adumbrates the conflict between the strict principle and the adjustment principle, a concept of reasonableness that has recently attained some prominence, primarily through the efforts of Lord Denning,[63] is the culmination of the adjustment principle. Fundamental breach as a 'rule of law', fundamental breach as a 'rule of construction' and reasonableness are themselves instances of the recurring theme of the adjustment of performance-related risks.

The progression of the concepts reflects to some extent the intuitive attempts by the courts to adjust performance-related risks. Fundamental breach as a 'rule of law' was regarded as unsatisfactory because it could not treat exception clauses discriminatingly; exception clauses applied or did not apply according to whether there was a fundamental breach. Fundamental breach as restated in *Harbutt's Plasticine*, it was thought, did virtually the same thing with an added (at times unreal) option to the aggrieved party to affirm the contract despite the fundamental breach and to assume the performance-related risks covered by the exception clause. In shifting performance-related risks from the performer to the other, both statements of fundamental breach also rigidly deprived the performer of all the protection of his exception clause even to the extent

62 Standard form contracts or adhesion contracts (when they are unilaterally drafted and imposed on the other party) are, to use Bright J.'s criteria, marked by two features: (i) one party has fixed unalterable conditions in advance, and (ii) the other either in ignorance or out of necessity submits to them The terms may be fair or unfair or they may be some or all of the conditions; "Contracts of Adhesion and Exemption Clauses" (1967) 41 *A L J* 261. In Watkins v. Rymill (1883) 10 Q.B.D. 178 at 188 per Stephen J., the emphasis is on the unilateral determination of the terms by one party Similarly, the originator of the term 'adhesion contract', Saleilles, spoke in terms of preformulated stipulations in which the offeror's will is predominant and the conditions are dictated to an undetermined number of persons and not to one individual party (as translated in the opinion of Henningsen v. Bloomfield Motors 161 A 2d 69 (1960) The Israeli legislative definition of a standard form contract is "a contract all or any of whose terms have been fixed in advance by or on behalf of the person supplying the commodity or service with the object of constituting conditions of many contracts between him and persons undefined as to their number or identity": Standard Contracts Law 5724, 1964, s 1.

63 Gillespie v. Roy Bowles [1973] 1 All E.R. 193 (C A.), Levison v. Patent Steam Carpet Cleaning [1977] 3 All E.R. 498 (C.A.), and Photo Production v. Securicor Transport [1978] 1 W.L.R. 856 (C A.) See also the unreported case of Bahous v. Alcor International (C A) July 1976.

that it might be directed at lesser breaches. A 'rule of construction' avoided the blanket operation of its predecessors and purportedly had the flexibility for a more discerning and discriminating adjustment of risks. It is potentially capable of giving due regard to the various kinds of exception clauses and transactional contexts. But a flexible 'rule of construction' was inadequate without some guidelines or standards by which the performance-related risks of exchange may be appropriately adjusted. Hence arose the concept of reasonableness which seeks to supplement the inadequacies of a 'rule of construction' and to enable courts to deal openly with the problem, unencumbered by doctrinal niceties.

Briefly the court will not allow a party to rely on an exception or limitation of liability clause in circumstances in which it would not be fair or reasonable to allow reliance on it, even if a clause in its natural and ordinary meaning would give exception from or limit liability for a breach.

The emergence of reasonableness is certainly influenced by the inadequacy of the law in the treatment of exception clauses as perceived by Lord Denning. Indeed the argument for its recognition is that in practice courts determine the contractual intention according to the reasonableness of the clause. It was only their reluctance to acknowledge openly the real or actual grounds of decision that has resulted in the array of difficult linguistic distinctions, confused constructions and massive conceptualisms such as the 'implied intention', the 'presumed intention' and the 'contemplation of the parties'. Reasonableness is the "principle which lies behind all our striving"[64] and represents a break away from the strained constructions that obscure the actual processes by which and the true grounds on which courts decide whether an exception clause may be relied on. The pretence that construction is explicitly or implicitly based on the contractual intention of the parties is abandoned. Reasonableness emerges in a straightforward manner to establish its own principles. Reasonableness would therefore avoid the practices which "do not truly represent the ways in which the courts act."

The most significant advantage of the concept of reasonableness is its abandonment of covert considerations. It deals openly with the social and economic matrices which constitute material considerations in many cases but which have hitherto been obliquely acknowledged, if at all.

Viewed against the theme of conflict between the strict principle and the adjustment principle, the concept of reasonableness represents a visible movement of the law away from the strict principle. No longer rivetted on the letter of the contract, the judicial mind is now receptive to the

64. Photo Production v Securicor Transport, supra n. 63, at 865.

unspecified] alternative means" already available in contract law provides an adequate and effective means of control.[70]

A Critique of Coote's Theory[71]

It is questionable if exception clauses are mostly substantive, that is, that they prevent obligations from accruing. The juristic function, we are told, is only one of the factors to be considered when determining the obligations of the parties. Whether the juristic function of a Type A clause prevails to prevent an obligation from accruing or whether 'the other considerations' supersede it, such that, despite the juristic function, the obligation in question accrues, cannot be determined *in vacuo*. The question, Coote says, "can only be answered by reference to the particular contract interpreted as a whole in the light of the surrounding circumstances".

The limits of the theory are quite clear. It does not elucidate how a judge should rate the juristic function with the other considerations.[72] Nor does it indicate what those other considerations are. How would the juristic function feature in, say, *Karsales* v. *Wallis*? There the hire-purchase agreement stipulated that "no condition or warranty that the vehicle is roadworthy or as to its age, condition or fitness for any purpose is given by the owner or implied . . .". The Buick car had upon inspection by the hirer been found to be in excellent condition. When delivered it was in a "deplorable condition", incapable of locomotion and barely resembled the car which the hirer had inspected. Various parts of the car had been removed or replaced with defective or old ones.

If the juristic function of the clause was to prevail, the owners would be under no obligation in respect of all that was stipulated in the clause. D. Jenkins, for example, thought that this was the effect of the clause but did not suggest what the plaintiff did promise to do. Subsequently he commented that if the deficiencies of the object tendered had been less flagrantly manifest so that though unroadworthy it was still a car, the result of the case would probably have been different.[73] Does this not presume that the hire-purchase was of a car, and a car with the usual attributes? And is this not contrary to what he thought was the effect

70 Id at 347

71. See also the book review by Treitel, (1964) 8 *J Soc Pub T L* , 12; Wright in 'Exclusion Clauses Rationale and Effect' (1972) 122 *New L J* 490 finds it "unacceptable" and attempts to show that Coote's argument that the obligations of the contract are those which the exclusion clause does not delete, is "not a valid one". Moreover, according to Wright, the "only purpose" of an exception clause is to prevent the enforcement of rights and duties under a contract

72 See e.g. the argument by Palmer and Yates which does not really answer the question 'The Future of the Unfair Contract Terms Act 1977' [1981] *Camb L J* 108 at 121

73. 'The Essence of the Contract' (1969) 28 *Camb L J* 251 at 263-266.

of the clause? If not, why does the clause not prevent the accrual of the obligation when the breach was less flagrant as it did in the first instance?

Even if the juristic function overrode all other considerations the contract was not necessarily illusory: it could be a contract for the hire-purchase of a wreck for which the hirer may have use as scrap metal, or it was one for a chance that the car may indeed be a car. Either of these two mutually exclusive interpretations is tenable. But in the light of the 'intent of the transaction' (or what is sometimes called the contemplation of the contract as distinguished from the parties' individual understanding),[74] in this case the hire-purchase of a car, the juristic function of the exception clause cannot prevail. The contract is for a car which therefore must have at least the ordinary attributes of a car. Here the delivery must indeed be that of the specific Buick car in the same condition at the time of its inspection. The exception clause therefore does not define the contractual duties of the owner but rather attempts to exclude his liability for breach of specific, though wide, aspects of his duty under the contract. In which case the effect of the exception clause remains quite a separate issue. It becomes clear from the foregoing that a distinction, which Coote doubts, between exception clauses which define contractual duties and exception clauses which exclude liability for specific aspects of contractual duty, is valid.[75]

In a sense then, one looks, as Lord Denning said in *Karsales* v. *Wallis*, at the contract without the exception clause if only to determine the 'intent of the transaction'. It is precisely in relation to this intent that various considerations including the juristic function may be weighted, the nature of the exception clause determined, and the content of what has been agreed on arrived at. The intent of the transaction would therefore be a very first consideration in the court's interpretation of a contract. In *Karsales* v. *Wallis* itself Lord Denning referred to, inter alia, *Spurling* v. *Bradshaw* where he had considered the contract in toto. This is clear from his observation in the latter case that if the exception clause was taken literally, there would be no contract. It is submitted, that one ought not to put undue literal emphasis on Lord Denning's statement in *Karsales* v. *Wallis* (to the effect that one looks at the contract apart from the exception clauses). Admittedly such a pointed statement is awkward as well

74. Dahl v. Nelson (1881) 6 App.Cas. 38 at 69; Becker v. London Assurance Corporation [1918] A C. 101 at 112.

75. In Kenyon v Baxter Hoare [1971] 2 All E.R. 708 at 711 Donaldson J. distinguishes three types of protective conditions. (i) those which limit or reduce what would otherwise be the defendant's duty, (ii) those which exclude liability for breach of specific aspects of that duty, and (iii) those which limit the extent to which the defendant is bound to imdemnify the other in respect of consequences of breach of that duty; see Coote, 'Discharge for Breach and Exception Clauses since Harbutt's "Plasticine"' (1977) 40 *Modern L Rev.* 31

forthright adjustment of the relative exchange positions of the parties. In the meantime there has been a spectrum of covert compromises between the strict principle and the adjustment principle evident in the preoccupation with the niceties of words.

Coote's Theory Explained[65]

The basic assertion of Coote's theory is that a promise which, by the use of an exception clause, is made at all times wholly unenforceable cannot give rise to a contractual obligation. For an exception clause which makes purported contractual rights wholly unenforceable is in effect preventing those rights from coming into existence in the first place. This is because there is no legal right if there is no legal liability.[66]

Exception clauses affect rights conferred by a valid contractual promise. These are a substantive "primary right" to performance of the contractual promise, a substantive "sanctioning right" to pecuniary compensation by the other who breaches his obligation, and a "procedural right" of enforcement of the sanctioning right. Thus exception clauses are substantive or procedural according to the rights they affect. Most of them, Coote suggests, place substantive limitations on the rights to which they apply and accordingly help to delimit and define those rights.

All exception clauses therefore fall into one of two categories according to their true juristic function, both of which affect the rights concerned from their inception. There are the exception clauses which directly or indirectly determine the content of a contractual promise. Coote refers to them as 'Type A' exception clauses. They generally affect substantive rights. But even an exception clause which affects a procedural right can be of the Type A variety if it renders that right wholly unenforceable because it in effect *prevents* the corresponding obligation from coming into existence. The significance of a Type A clause is that an alleged breach may turn out to be no breach at all, there being no obligation which could have been breached. The other category comprises exception clauses which *qualify* 'primary' or 'secondary' rights without preventing the accrual of any particular primary right. These are the 'Type B' exception clauses which merely qualify rights that do accrue.

In most cases, according to Coote, exception clauses are of the Type A variety, defining the rights or promises to which they apply. Where they do affect the accrual of obligations they obviously cannot be regard-

65. B. Coote, *Exception Clauses* (1964).

66. The basic assertion is supported by analogies drawn from other contexts which suggest that the parties to a contract cannot voluntarily create an unenforceable 'duty' at common law. Any such 'duty' can only be brought about *ab extra* by statute.

ed merely as defences or shields to claims for damages for breaches of existing obligations.

A consequence of the juristic function of Type A clauses is that exception clauses must be considered with the rest of the contract at the stage when a court determines what obligations were intended and in fact created, and how much of what transpired between the parties has become part of the contract. Thus to look at the contract, as suggested in *Karsales* v. *Wallis*, "apart from the exempting clauses and see what are the terms, express or implied, which impose an obligation on the party"[67] is unsound. This is Coote's first assertion, that is, it is wrong to assume that all exception clauses are only defences or shields to claims for damages thereby perpetuating the fallacy implicit in *Istros* v. *Dahlstroem*,[68] namely, that one may voluntarily create an unenforceable duty.

Coote's case on exception clauses starts from the premise that the courts' traditional role is to uphold the 'primacy' of contracts: they are to uphold the intentions of the parties as gathered from the words. This means that in view of their true juristic function exception clauses must be interpreted together with the rest of the contract and according to the ordinary rules of interpretation. Putting this differently, courts are to take contracts at face value and to subject them only to the rules hitherto developed to guide or assist interpretation or to fill gaps. The point of the Type A and Type B distinction is therefore that the existing rules of construction are more likely to affect the Type A than the Type B ones.

But subsequently in a well known and highly regarded article published after the publication of his monograph Coote conceded that judicial control of exception clauses may also be desirable in order to "protect the weak from cynical and harmful exploitation".[69] This is a fundamental concession to the bargaining relationship between the parties to a contract. It is also a compromise of the strict principle: interpretation must now take into account the relative positions of the parties in a bargain.

The concession is, however, a limited one as he insists that the law must not be perverse and become an arm of public law. Since, according to him, exception clauses are primarily economic, no arbitrary rule, that does not discriminate between cases where exception clauses are aimed at defeating reasonable expectations and those which are attempts to allocate risks, should be allowed to bar their operation. Where interference is desirable, an approach based on the true juristic function of exception clauses, together with the "very potent and more soundly based [but

67 Per Lord Denning in Karsales v. Wallis [1956] 2 All E.R 866 at 869.
68. [1931] 1 K.B. 247.
69 ' The Rise and Fall of Fundamental Breach' (1967) 40 A.L.J. 336

as misleading. But in the majority of cases the intent of the transaction is very much a part of the ratiocination although it is determined implicitly and inconspicuously by the courts.

Because of its very nature it would seem that the concept of the true juristic function is likely to be superseded in many cases by other considerations. The case against its emphasis is compelling. It must not be overrated as undue weight may be placed on matters of form which will in turn facilitate the evisceration of the contract. Emphasis will be shifted to linguistic formulations and their Hohfeldian or Austinian meanings rather than to the contract as a viable commercial transaction.[76] Adherence to the legalistic phraseology of a contract will not produce commercially satisfactory results especially since laymen can hardly be expected to understand legal formalism. How easily a court may be led to overemphasise matters of form is indicated in *Munro Brice* v. *War Risks Association*.[77] There Bailhache J. used a distinction between two types of exception clauses similar to Coote's Types A and B clauses for the purpose of determining the onus of proof. He admitted the distinction was very much a matter of form. A promise with exceptions could generally be turned into a qualified promise by a mere alteration in phraseology.[78]

The implication of the exception clause form itself may militate against the importance of the juristic function. As Coote notes, the use of an exception clause suggests a wider initial promise followed by an exception which can be either an excuse (defence function) or, equally plausible, a negation of certain parts of the promise. As the logic of the juristic function only operates from certain premises to the correct conclusion and is incapable of selecting the premises it does not indicate that it should be preferred to the defence function. On the contrary a court may be persuaded to think less of the juristic function of an exception clause because its form tends to mislead a party into thinking he has more rights than is actually the case by restricting rights apparently conferred by other parts of the contract.[79]

If the 'juristic function' is the only relevant consideration then it will be possible to conclude with Coote that in a contract for the sale of a

76 As Holmes said, "the most important element of decision is not any technical, or even any general principle of contract, but a consideration of the nature of the particular transaction as a practical matter . . the immediate legal effect of what the promisor does is, that he takes the risk of the event, within certain defined limits, as between himself and the promisee" *The Common Law* (1881, 1968 reprint).

77. [1918] 2 K.B. 78

78 In T N T. v. May & Baker (1966) 115 C L.R 353 at 385 Windeyer J. said that whether a clause is one or the other depends on the words. Contra the approach adopted by the majority at 360 and 365.

79 The Law Commission and the Scottish Law Commission, *Exemption Clauses*, Second Report (1975) (No.69) para. 143-146.

specific motor-car described as a 1948 model an exception clause that "the vendor shall not be liable for any error of description whatever" negates a promise to deliver a 1948 model, in the same way as if the clause had stated that "the vendor gives no undertaking whatever, contractual or otherwise, that the car is a 1948 model and the statement that it is a 1948 model is intended to be only a mere representation not forming part of the contract". But in the light of the intent of the transaction and the circumstances of the case, it may be more easily concluded that the first exception clause is a mere defence or excuse not affecting the seller's obligation to sell a 1948 model. Such a conclusion will not be 'absurd' if the juristic function is justifiably superseded by other considerations.

In practice so far, judges have not noticeably attached too much importance to the juristic function. Coote himself foresaw that the future development of the law was unlikely to follow an approach based on it. In a wider context there is no particular evidence of judicial fervour for legalistic technicalities that may suggest a more receptive attitude towards the juristic function in future. Judicial rhetoric to the effect that surely the parties could not have intended the technical effect of a clause, and the fundamental postulate of common law, that the parties to a contract are deemed to be reasonable men, diminish the importance of the 'juristic function' of exception clauses. As Llewellyn has put it succinctly, in a contract "what has been assented to, specifically, are the few dickered terms and the broad type of transaction and a blanket assent (not a specific assent) to any not unreasonable or indecent term the seller may have made on his form, which do not alter or eviscerate the reasonable meaning of the dickered terms".[80] On this view, it is difficult to imagine that parties to a contract would intend to assent to the use of juristic technicalities to attain such an end. Besides if contract law is to reflect the commercial practices of businessmen it must not constitute an increased source of risk by diverging from lay expectations and understanding. Modern trends in other aspects of the law are not inclined to overesteem juristic technicalities. For example, there is as represented in *Hongkong Fir Shipping* v. *Kawasaki Kisen Kaisha* a discernible trend away from the technical nomenclature of 'warranty' and 'condition'.[81] There the effect of a breach was said to depend on the seriousness of the event that flowed from the breach and not on the traditional *a priori* classification of the term breached. This approach was taken further in *Schuler* v. *Wickman*,[82] and in *Hansa Nord*[83] where the House of Lords and the Court of Appeal respectively

80 (1939) 52 *Harv L Rev* 700
81 [1962] 2 Q B 26
82 [1974] A.C. 235 (H L.).
83. Cehave v Bremer Handelgesellschaft [1975] 3 W L.R 447

held that even if a stipulation is expressly described in the contract as a condition, this is not necessarily determinative of its effect. In the last analysis the appropriateness of a remedy for the breach in question determines if a broken term is a condition.[84] Further, in *Reardon Smith Line* v. *Sanko Steamship*[85] the House of Lords indicated that nineteenth century sale of goods cases should nowadays be regarded as excessively technical and were due for re-examination.

The most important consideration for present purposes is the implications of the juristic function of exception clauses for our theory of performance-related risks. By Coote's reckoning, exception clauses in most cases prevent rights from accruing in the first place and consequently an issue of breach does not arise. Coote further contends that if any control of exception clauses is for whatever reason desirable, an approach based on the juristic function is capable of ensuring adequate control. We shall consider each point in turn.

We have already seen, that a distinction may be made between a formative question of the validity and content of a contract and a 'performatory' question of the relationship between the parties in the event of a breach. Coote's preoccupation with the former is evident in his argument that had the 'juristic function' of exception clauses been acknowledged by the courts, it 'would have been apparent that no exception clause can wholly exclude liability for breach of either warranty or condition'. [86]

According to Coote, when a court assumes that a Type A exception clause (i.e. one which prevents an obligation from accruing) is a mere defence or excuse, it gives to an apparent promise a substance which it does not have. In addition, it finds itself still confronted with the problem of an all-embracing exception clause. In order to limit the exception clause the court then resorts to the difficult concept of 'difference in kind' which prescribes that an exception clause cannot be relied on by the performer if the performance rendered was 'different in kind'. This reasoning, Coote argues, is artificial and can be avoided by an approach based on the juristic function of exception clauses. The agreement, he says, may be found to be not a contract at all if the exception clause is so wide as to negate all contractual obligation. Or if the court decides

84. In Schuler v Wickman [1974] A C 235 at 251 Lord Reid said "The fact that a particular construction leads to a very unreasonable result must be a relevant consideration The more unreasonable the result the more unlikely it is that the parties can have intended it, and if they do intend it the more necessary it is that they should make that intention abundantly clear". Lord Morris and Lord Simon thought that it would otherwise be "absurd" and "fantastic" respectively at 255-6, 265, Lord Kilbrandon was concerned over the "unreasonable results" and "grotesque consequences" if the contrary was the case, 272; cf. Lord Wilberforce (dissenting) at 263

85 [1976] 1 W L R 989 at 998 and 1001

86 It is also evident in his criticism of the notions of fundamental breach and 'difference in kind' in Smeaton Hanscomb v Sassoon I Setty

that the agreement is contractual "then *a fortiori* an ascertained subject-matter is something that the exemption clause cannot be allowed to exclude. Particularly where the contract is for a sale by description, the courts would . . . [be] obliged, to restrict the literal meaning of the words used in order to leave some element of contractual definition".[87] The irreducible content of the contract is consequently determined without the difficult concept of difference in kind and by a means which ought to give greater flexibility. Consequently the question of whether a Type A exception clause can enable a seller to deliver goods different from those contracted for does not arise at all. It follows too that a Type B exception clause is not affected as it does not prevent the accrual of obligations. There is, Coote says, nothing to suggest that the unexcludable minimum is less than that arrived at by the concept of 'difference in kind'.

It is true that when an exception clause purports to qualify a promise *qua* promise so as to render the contract illusory, it is a question of ascertaining from all the circumstances including the juristic function whether the parties did in fact enter into contractual relations. If the court finds that they did despite the juristic meaning of the exception clause, the next task is to determine the content of the contract or the substance of the promises. Insofar as the validity of the contract is concerned, it is only necessary that two sets of promises are given for each other. However, in order to support each other, the promises must have a certain content. But as adequate consideration is not a prerequisite of a valid contract, the promises need only have some content. So far, the issue is still one of the validity of a contract. To this issue the notion of performance-related risks is not relevant.

Strictly speaking, to determine whether a valid contract exists the courts need only find that the promises have *some* content. But since a dispute almost invariably comes before a court after an alleged breach, a question posed is whether an aggrieved party may rescind or is entitled to damages. In order to decide that, the entire content and consideration of the contract must be ascertained, for any right to rescind must be decided in the context of the entire consideration. Here too, the concept of performance-related risks is not necessary to ascertain the entire content and consideration of the contract just as they are not concerned with the validity of contracts.

Our theory of performance-related risks is instead concerned with any qualification by the performer of liability for avoidable misperformances of that which he has promised to perform. It marks out the circumstances under which a performer will, despite an exception clause which *prima*

87 Coote, Supra n.65 at 55-56.

facie protects him, be made liable for his default. The issue is subsequent to and different from the issue of what obligations the parties have undertaken. The obvious fact is that performance-related risks are important where, despite the juristic function of exception clauses, it is found that an exception clause does not prevent obligations from accruing but protects a performer from misperformances of certain aspects of his duty. For example, the concept of 'difference in kind' which the courts have developed therefore denotes the limit beyond which a contract becomes illusory; not in the sense of an illusory promise to perform or a potestative condition but in the extended sense of not taking care to do that which he has promised to do.

Coote's argument does not share the thrust of performance-related risks. It is also erroneous to think that in answering the question of the validity and content of the contract one has somehow also answered the subsequent question of what kind of performance must be given. This is not an uncommon mistake. As a consequence, the problem has generally been wrongly regarded as one of 'construction'. The truth of the matter is that performance-related risks strike at the very basis of the institution of the bilateral contract and set out the limits of the extent to which a performer may protect himself from the outset with a wide exception clause and then unilaterally increase the payor's 'normal' share of performance-related risks.

The main advantage of an approach based on the juristic function of exception clauses, according to Coote, is that it can "concentrate the forces at the [judge's] disposal" where a court might wish to limit the effect of a particular exception clause. If, after weighing all the circumstances including the exception clause, the court should decide that, despite the presence of the exception, a particular term was intended to have effect, it will for that very reason be able to hold that the exception clause cannot apply. The "overall contractual intentions can be combined with the restrictive rules of interpretation to temper and confine the words of the exception clause".

We have already noted the ambiguity surrounding the task of weighing the juristic function and other unspecified considerations to decide what obligations have accrued. This ambiguity is not now alleviated. On the contrary the juristic function is perhaps made more precarious in its operation. For the suggestion seems to be that for the purposes of controlling an exception clause the importance of the juristic function ought to be played down. This in turn means that ultimately what really matters are the reasons for which courts will exercise any desired control. And the juristic function is no more than a convenient means to attain the goals of control. The significant advantage claimed for Coote's approach

therefore amounts to (in theory, at least) a supposedly more acceptable reason (that it was the 'parties' intention) for judicial interference. Presumably the court can say it was the contractual intention of the parties that an exception clause was not to apply, thus avoiding the need to justify its interference. Presumably too, a court, which decides for whatever reason that judicial control of an exception clause is desirable, can more easily interfere with and adjust the contractual relationship at the stage when it determines the obligations said to be undertaken. It will give the appearance of neat conceptual synthesis with the traditional view of Anglo-Australian contract law as a systematised or homogenous law based on the consensus of the parties. It will probably allow the court more room to manoeuvre the control of such clauses than would be the case if the conclusion was arrived at by some fixed principle of law.

Checking excessive exception clauses through the juristic function has a serious weakness. As it resolves the problem at the stage when the content of the contract is determined, it emphasises the language used. Eventually one is forced into the pursuit of the 'right' or 'appropriate' words typified in *Andrews* v. *Singer* and *L'Estrange* v. *Graucob*. A theory of performance-related risks, by contrast, can take into consideration a whole scale of different kinds of misperformance together with all the circumstances of the case from both the seller's and the buyer's points of view. Indeed even a theory of the true juristic function is not free from a notion of performance-related risks. It was observed in *The Angelia* v. *Iino Kaiun Kaisha*,[88] a case which is often cited to support Coote's theory, that in deciding whether the juristic function prevails an important consideration is whether the events in which an exception clause operates are beyond the control of the performer. If they are, the clause is likely to be regarded as a provision defining the contractual duty rather than one excluding liability. Thus in *Renton* v. *Palmyra Trading Corporation*[89] Jenkins L.J., in allowing a provision for a substitute performance, said that "the distinction is between a power given to one of the parties which, if construed literally, would in effect enable that party to nullify the contract at will, and a special provision stating what the rights and obligations of the parties are to be in the event of obstacles beyond the control of either arising to prevent or impede the performance of the contract in accordance with its primary terms".

Taken on its own terms, Coote's approach has several other limitations. A theory of the juristic function of exception clauses alone does

88 [1973] 2 All E.R. 144 at 162-163.

89. [1956] 1 Q.B. 462, at 502, quoted in [1957] A.C 149 (H L) at 164 A contract for the shipment of timber from Canada to London contained a clause which provided that "the Master may discharge the cargo at . . . any other convenient port" if strikes prevented discharge at the named ports

not indicate two essential things, namely, when and how an exception clause should be controlled. The sum of Coote's proposition seems to be that judges must uphold the primacy of a contract, but if in the circumstances control is desirable they can exercise such control more freely with whatever expertise they may chance to possess in the matter of the distribution of loss or whatever else they see as the goal of control. The wisdom of such a proposition is dubious. First, how control will proceed turns on the questionable skill of individual judges to achieve such an end via an approach which is likely to depend too much on the language used. Unless it can be said that judges are somehow imbued with a consistent conception of the goal of intervention which both reflects and evolves with changing and accepted social and/or economic values, this must surely be a serious weakness in the theory. Even if the goals are understood, as Mr. Justice C.H.Bright confessed in his discussion of adhesion contracts, "judges, particularly judges long removed from fields of commerce, are [not] always well fitted to decide what is 'fair' or 'unfair' ".[90]

Second, it would mean that the 'true' reasons for control are deliberately disguised or buried under a bulwark of linguistic technicalities. Third, these ramifications are in any event inconsistent with Coote's condemnation of arbitrary judicial interference. Quite clearly to avoid such a state of affairs there ought to be some policy or policies in accordance to which Coote's approach may be wielded by judges in the control of exception clauses.

Fourth, to the extent that Coote's approach based on the 'juristic function' admits judicial control of exception clauses, predictability and certainty in the law depend not on the juristic function of exception clauses or the contractual intention as evidenced in the contract, but on the circumstances in which or the reasons for which a court will interfere. Fifth, and ironically, to the extent that the court does and will interfere, the importance of the 'juristic function' of exception clauses is diminished.

Finally, any judicial control of exception clauses based on Coote's approach may in practice prove to be very circumscribed. For its operation is limited to only Type A clauses since Type B clauses do not affect the accrual of obligations. A very obvious way to avoid the judicial probe is of course to use a Type B clause; instead of excluding his liability, a performer can limit it substantially. A possible answer is, as he suggests, to regard a Type B clause as *prima facie* having no effect in limiting claims based on a failure by the seller to deliver goods of the contract description on the ground that it contains 'general words' of exclusion. That be-

90 'Contracts of Adhesion and Exemption clauses' (1967) 41 *A L J* , 261

ing the case, the 'general words' should be interpreted as not affecting recovery for (for instance) negligence or for breaches of the more important implied-by-law terms.[91] But this rather cosmetic suggestion does not really meet the case. For ultimately the court cannot go beyond a clear prescription to the contrary by the language in context. Indeed this very limitation highlights the essentially semantic nature of Coote's approach. Thus a performer can by limiting his liability to a derisory sum effectively minimise his commitment to perform.

It is of course arguable that implicit in Coote's first premise, namely, that courts must uphold the primacy of contracts, is a policy for the control of exception clauses. It would follow from this that any judicial control that operates through the juristic function of exception clauses and tampers with obligations which the parties on the face of the contract have undertaken, is only justifiable where the contract is concluded in consequence of some objectionable circumstance which may be said to affect the element of agreement. Examples foreseeably include the existence of oppressive practices and the abuse of bargaining power in the procurement of contracts. The justification would presumably be along this line: that freedom of contract and sanctity of terms to be meaningful must connote some choice. For it is only in circumstances similar to those just mentioned that the primacy of contract is not undermined. Apart from these, control will be theoretically inconsistent with the primacy of contract. Coote's approach would therefore be directed at a completely different problem from that which our theory attempts to resolve. It leaves untouched precisely the task of determining the types of risks of avoidable misperformance which a performer may impose on the other party.

A Sketch of a Theory of Risks of Avoidable Misperformance

To make a bad bargain is to sell too cheaply or to buy too dearly, but courts do not, in accordance with established law, review a bargain to ensure that it is adequate. Nor are they now required to do so by a theory of risks of avoidable misperformances or performance-related risks.

The theory seeks to indicate how a performer must have performed before he can be protected by an exception clause from his own avoidable mis-performance. There is in the cases an intuitively differentiated conception of performance-related risks: courts examined the quality of the performer's avoidable misperformance where it resulted in the total collapse of the bargain, to decide if an exception clause which was *prima facie* wide enough to protect him would nevertheless be overridden. So that an exception clause was excessive or overwide only in the sense that

91 Coote, supra n 65, at 57-59

it excused the performer whose default was tainted by some degree of culpability and which deprived the other party of his bargain.

A theory of performance-related risks therefore contends that although a contracting party usually accepts certain risks of misperformance where he has agreed to an exception clause, he does not accept all risks which are semantically within the ambit of the clause. This theory is apt to explain, in particular, the sale of goods and hire-purchase cases in which much confusion has arisen because the two questions, of what was agreed to be sold and the kind of performance that must be given before an exception clause which *prima facie* excuses the performer can be relied on, have been treated without distinguishing them. We shall therefore, look at the types of performance-related risks that may be gathered from the cases. The key decision of *Wallis* v. *Pratt*[92] is generally thought to have decided that no contractual term is immune from express exception. The application of an exception clause, it seems, would in every case turn on the exactitude and appropriateness of the express language used. But another interpretation of *Wallis* v. *Pratt* suggests that risks of certain qualities of misperformance by a seller may not be passed to the buyer. According to Lord Loreburn:

> There is no doubt that when you are dealing in a commodity the inspection of which does not enable you to distinguish its exact nature, there are risks both on the buyer and the seller . . . But if it is desired by a seller to throw the risks of any honest mistake on to the buyer, then he must use apt language.[93]

Implicitly, where the misperformance involves latent defects (even those which are so gross as to make the goods different in kind) the seller may pass to the buyer the risks of his 'honest mistake'.

Although little notice has been taken of Lord Loreburn's idea, the sum effect of it and subsequent cases as *Pinnock* v. *Lewis & Peat*, and *Smeaton Hanscomb* v. *Sassoon I. Setty* may be stated this way : a performer cannot shift risks of his own avoidable misperformance that is 'different in kind' to the buyer. The only exception is the risk of an 'honest mistake' which he may shift to the buyer where the defects are latent.

A more recent development of Lord Loreburn's idea is to be seen in *Green* v. *Case Bros. Farm*[94]. That was a case where twenty tons of uncertified King Edward potatoes sold turned out to be unmerchantable because

92 [1911] A C. 394.
93 Id at 396.
94 [1978] 1 Ll L R 602; Ziegal, 'Contracts — Doctrine of Fundamental Breach — Effect of Disclaimer Clauses — the Beginning of the End?" (1979) 57 *Can Bar Rev.*, 105

of a latent virus. The source of the unmerchantability was, however, not finally diagnosed until some nine months later. The sellers sued for, inter alia, the price and the buyers counterclaimed for a total loss of profit on the crop planted of about ten times the price of the potatoes. The sellers sought to rely on two exception clauses which required the buyers to give notice of their claim within three days of receipt of the potatoes and which limited the sellers' liability to the price of the potatoes. Griffiths J. disallowed reliance on the first clause but upheld the second. Under s.55(4) Sale of Goods Act 1893 an exception clause which exempts unmerchantability cannot be enforced to the extent that it would not be fair and reasonable to allow reliance on it.

The sellers could not reasonably rely on the time clause becuase the buyers could not be expected to complain within three days of delivery of a latent defect which they did not become aware of until much later. It was, however, reasonable to allow reliance on the limitation of liability because, among other reasons, neither party was morally blameworthy and neither knew or could be expected to know of the infection.[95]

Risks of defects discoverable on examination, where ample opportunity for examination is provided, are on the buyer. For example, a buyer has to bear the risks of the seller's delivery of barrels of unmerchantable glue, which defect he would have discovered if he had looked inside the barrels instead of merely examining the outside.[96] But in all other instances not involving honest mistakes, even where a seller possesses no special skill or on whom the buyer does not rely for expertise, the risks of latent defects are generally regarded as borne by the seller where the buyer is neither any better informed nor is in a position to be. Implicitly the seller is, perhaps by virtue of his trade, made to assume a higher duty of care. The quality of the conduct constituting the breach therefore has a relatively narrow significance. This may be explained by the nature of the obligation involved in sale of goods and hire-purchase where the contract is for the delivery of things in a certain state rather than, say, for the conduct of some activity. So that notions of doing one's best or acting diligently rarely arise; the evaluation of the quality of performance here coincides with a preceding question of whether there was performance of the contract at all. The risks of avoidable misperformance against which the seller cannot be protected are those of a tender of goods 'different in kind'.

95 There was even a clause explaining the need for the limitation of liability "Seed potatoes sometimes develop diseases after delivery. It being impossible to ascertain the presence of such diseases by the exercise of reasonable skill and judgment the Seller cannot accept any responsibility should any disease develop after delivery other than as provided under [this] clause"

96 Thornett & Ferr v Beers [1919] 1 K.B 486. Cf Grosvenor Motor Auctions [1960] V R 607

Bailments

In bailments on the other hand, the culpability of the avoidable misperformance would seem to have more relevance. Indeed we have The Gibaud or 'four corners' rule fairly well established in contracts of carriage of goods by land and sea, contracts for the deposit of goods, contracts for laundering and drycleaning, and for towage.

The essence of the Gibaud rule is that a party to a contract cannot rely on an exception clause where he has not performed within the 'forner corners' of the contract. A much cited statement of the rule in *Gibaud* v. *Great Eastern Highway*, from which it derived its name, explains that:

> if you undertake a thing in a certain way, or to keep a thing in a certain place, with certain conditions protecting it, and have broken the contract by not doing the thing contracted for in the way contracted for, or not keeping the article in the place in which you have contracted to keep it, you cannot rely on the conditions which were only intended to protect you if you carried out the contract in the way in which you had contracted to do it.[97]

It is of course possible for two parties indisputably to enter into a contract for the *chance* that the other *may* perform his obligations in which case the very essence of the contract is the total assumption by one party of all risks of non-performance by the other. But in all other cases, "[if] a bailee elects to deal with the property entrusted to him in a way not authorised by the bailor, he takes upon himself the risks of so doing except where the risk is independent of his acts and inherent in the property itself".[98] That this was the law had been left in little doubt in *Garnett* v. *Willan*[99] which was decided a hundred years earlier. In that case where carriers conveyed goods by a means other than that stipulated by the contract, it was held that an exception clause similar to that in *Gibaud* v. *Great Eastern Railway* could not be relied on. Bayley J. noted that a carrier was entitled to limit his responsibility to a reasonable extent since he ought to have compensation in proportion to the value of the article entrusted to his care and the consequent risk which he runs. He could not, however, excuse himself from the consequence of his own "misfeasance".[100] Thus, while the exception clause would be construed

97 [1921] 2 K.B 426 at 435 per Scrutton L J., Wade, 'Artıcles Left at Station' (1921-23) 1 *Camb L J* , 86; M J.G., 'The Four Corners of a Contract' (1962) 106 *S J* , 341.

98. Per Grove, J. in Lilley v. Doubleday (1881) 7 Q.B.D 510, at 511.

99. (1821) 5 B. & Ald. 53, 106 E.R. 1113; Sleat v Fagg (1822) 5 B & Ald. 341, 106 E R. 1216. Earlier cases cited ıncluded Bodenham v Bennett, 4 Prıce 31, 146 E.R. 384, Bırkett v. Willan 2 B & Ald 356, 106 E R. 397.

100 (1821) 5 B & Ald 53, 106 E.R. 1113, at 1115

to give him the protection he "ought to receive" it was subject to his not doing anything "by his own voluntary act, or the act of his servants, to divest himself of the charge of carrying the goods to the ultimate place of destination".[101]

The 'four corners' of a contract must necessarily depend on the nature of the contract in question. Consequently the 'four corners' is a criterion that takes many forms in a variety of fact-situations. It is proposed to describe here the 'four corners' of the types of contracts to which the rule has been applied so far.

(a) Carriage of Goods by Sea

In these cases deviation from the agreed route or where none was stipulated, the customary route, was a prime example of an act outside the 'four corners'. Deviation provided a graphic example of a spatial quality of the 'four corners': 'stepping outside the four corners' was quite obvious.

A grave view was taken of deviation. The amount of damage resulting from it was immaterial. The moment deviation occurred, however inconsequential for practical purposes, the former was not allowed to rely on an exception clause. The mental state of the performer when deviating was also irrelevant. If "the route be abandoned, whether it was due to oversight, ignorance, accident, or design, equally the agreed transit is departed from, and the privileges the carrier enjoys by contract during that transit cease"[102]. In *Hain Steamship* v. *Tate & Lyle,*[103] for instance, a ship was chartered to load sugar at two Cuban and one San Domingo ports. The master of the ship was to be informed by telegram of the San Domingo port which was not at the time of the contract determined. Owing to the failure of the Cuban authority to deliver the telegram, the master set off for home after loading at the Cuban ports. When the mistake was discovered and the master was informed by wireless, the ship altered course to San Domingo. In doing so, damage to the ship and cargo was sustained. The House of Lords held the shipowner liable for deviation.

The Gibaud rule thus applied rigidly in cases of deviation. The performer was made responsible for virtually all damage when the ship deviated from the contract or usual route. He had the exceedingly heavy onus to show that had it not been for the deviation the damage or loss would still have occurred (and would have been excused) before he could

101. Id. at 1114 (Best J. distinguished between negligence and misfeasance)
102 L & N W. Railway v. Neilson [1922] 2 A.C. (P.C.) 263 at 269. This was a case of carriage of goods by land which applied the rule in deviation cases.
103. [1936] 2 All E.R. 597 (H.L).

be protected by an exception clause.[104] He might for instance show that the damage was the result of inherent vice.[105]

The reason for the stringent view taken of deviation lies in the historical development of the Gibaud rule which is said to hail from *Davis* v. *Garrett*,[106] the earliest reported English case of an action by a cargo owners against the shipowner. There, the master of the ship deviated unnecessarily from the usual course, during which a tempest wetted the cargo of lime and set the ship on fire resulting in a total loss. The ship-owner argued that there was no necessary proximity of causation between the deviation and the damage caused by the tempest and hence the cargo owner's averment of loss by unnecessary deviation was insufficient and proof of proximity had to be given. The case proceeded on the basis that deviation was a separate cause of action. Tindal C.J. held that there was a presumption of proximity between causation and damage and it was for the defaulting shipowner to negative it. The defaulting shipowner was responsible for the consequences that flowed from the deviation because he, the wrongdoer could not be allowed to "apportion or qualify his own wrong".

It is possible to interpret *Davis* v. *Garrett* to mean that the exception from perils of the sea in that case could not apply because the loss (presumptively) resulted from the deviation and hence was not covered by the clause. But Tindal C.J.'s decision turned on the fact that the loss happened while the *wrongful act of the deviation was in operation*. This was confirmed by Groves J. in *Lilley* v. *Doubleday* who also refuted the argument that *Davis* v. *Garrett* was decided on the ground that the shipowner was a common carrier.[107] Moreover, Tindal C.J. had in *Davis* v. *Garrett* further illustrated the point with an example uncomplicated by an exception clause: the "same answer might be attempted to an action against a defendant who had, by mistake, forwarded a parcel by the wrong conveyance, and a loss had thereby ensued; and yet the Defendant in that case would undoubtedly be liable".[108]

When similar facts arose in *Leduc* v. *Ward*[109] it was held that the ship was on a "voyage different from that contracted for to which the excepted perils clause did not apply". The noticeable shift of emphasis to the nature of deviation suggested that the fact of deviation ipso facto made excep-

104 E g Davis v Garrett (1830) 6 Bing. 716, 130 E R 1456, Scaramanga v Stamp (1880) 5 C.P.D. 295 at 299, 306 (C.A.); Morrison v. Shaw, Saville and Albion [1916] 2 K.B 783 at 795, 796, 800 (C.A.), Buerger v. Cunard S S. [1925] 2 K.B. 646 at 654, 659 (C.A); Hain Steamship v. Tate & Lyle [1936] 2 All E R. 597 at 606 (H.L)

105. Internationale Guano v. MacAndrew [1909] 2 K.B 360

106. (1830) 6 Bing 716, 130 E.R. 1456.

107 (1881) 7 Q.B D. 510 at 511

108 (1830) 6 Bing. 716, 130 E.R 1456 at 1459.

109. (1888) 20 Q.B.D. 475.

tion clauses inapplicable. This contributed to the subsequent view that a shipowner who deviates loses the protection of his exception clause as from the moment the deviation commences whether or not the cargo owner incurs increased risks of non-performance as a consequence. An illustrative example is *Joseph Thorley* v. *Orchis Steamship*. [110] The contract of affreightment contained a clause excepting the shipowner from liability for loss arising from, inter alia, the negligence of stevedores in loading and unloading the ship. The goods were damaged through the negligence of the stevedores when discharging the ship. The owners of the goods brought an action to recover the amount of the loss so occasioned. *Prima facie*, the damage was covered by the clause. Earlier, the ship had deviated from the contract route, but it was found on the facts that there was no relation between the damage and the deviation.

The rule in *Davis* v. *Garrett*, it was obvious enough, could not provide an answer in the goods owners' favour. The burden of risks that they bore in the normal course of events had not been increased by the deviation. The loss was not caused constructively by the deviation either. The court nevertheless held that the shipowner, by deviating, voluntarily substituted another voyage for that contracted in the bill of lading and consequently "cannot claim the benefit of an exception . . ., which is only applicable to the voyage mentioned in that contract".[111] By the deviation, it said, the shipowner had rendered the performance of something "fundamentally different".[112]. "The voyage actually carried out was a different voyage from beginning to end and therefore the whole bill of lading was gone".[113]

This twist in *Joseph Thorley* v. *Orchis Steamship* was the result of the judges' differing analyses of the "true principle' in *Balian* v. *Jolly*. Collins M.R. found that the undertaking not to deviate was a "condition precedent" to the right of the shipowner "to put the contract in suit". Hence it was unnecessary to show the nexus between the loss and the deviation. Cozens-Hardy L.J. on the other hand relied on what he considered was the precursor of *Balian* v. *Jolly*, the marine insurance case of *Lavabre* v. *Wilson*[114] where Lord Mansfield had said:

> The true objection to a deviation is not the increase of the risk. If it were so, it would only be necessary to give an additional premium.

110 [1907] 1 K.B. 660; see also Morrison v. Shaw, Saville and Albion [1916] 2 K.B. 783; Stag Line v. Foscolo [1932] A.C 328.
111. [1907] 1 K B. 660 at 669, per Cozens-Hardy L.J.
112. Id. at 669 per Fletcher Moulton L.J
113. Balian v Jolly (1890) 6 T L.R 345 (C.A.).
114. 1 Dougl. 284, 99 E R. 185.

> It is that the party contracting has voluntarily substituted another voyage for that which has been insured.

The contextual meaning of this passage on which Cozens-Hardy L.J.'s decision hinges, it is submitted, has been misunderstood. In *Lavabre* v. *Wilson* the issue was whether the insurance underwriters were discharged from their contractual obligations because the ship deviated. It was held that they were as the deviation was a unilateral alteration of the subject-matter of the contract, namely, the route insured. No exception clause was in issue. Support therefore could not be obtained from the passage cited for the imputation that special consequences flow from the fact of deviation *per se* in respect of all exception clauses regardless of their bearing on the deviation. Quite clearly Cozens-Hardly L.J. had given the passage an extended meaning in applying it to the facts of *Joseph Thorley* v. *Orchis Steamship*. This was fortified when some members of the House of Lords in *Hain Steamship* v. *Tate & Lyle*[115] subsequently stated the effect of deviation in similar terms. In this later case too no exception clause was in issue; the question being whether the cargo owners could opt to be discharged of their obligations under the contract for failure of consideration when the ship deviated from the contract route. Lord Atkin held that a deviation was a breach of such a serious character that, however slight, the other party to the contract was entitled to treat it as going to the "root of the contract", and to declare himself as no longer bound by any of its terms. The extremely grave consequence of deviation, he said, was justified by the fact that deviation vitiated the insurance and altered the subject of the contract. Lord Wright stated the "clearly established" law that deviation deprived the shipowner of his right to rely on contractual as well as common law exceptions and abrogated the entire contract.[116]

The substitution of one voyage for another thus became central to the question of whether exception clauses apply. Once there is a deviation, however slight, the exception clause does not apply. The concomitant idea was that deviation displaced the contract. It was said that "where there is a deviation the special contract . . . ceases to exist".[117] But the elliptical expressions that the contract, or the exception clause described as the "special contract" "ceases"[118] or "ceases to exist"[119] could not stand

115. [1936] 2 All E.R. 597 at 608, 612-614 (H.L.), U.S. Shipping Board v. Bunge and Born (1925) 42 T.L.R 174
116. Citing Morrison v Shaw, Saville and Albion supra n.110 and Joseph Thorley v. Orchis Steamship as authorities. The former was, unlike the latter, a straightforward application of Davis v. Garrett
117. Per Pickford J. in Internationale Guano v. MacAndrew [1909] 2 K.B. 360 at 365.
118. L. & N W. Railway v. Neilson [1922] 2 A.C. 263 (H.L.).
119. Internationale Guano v. MacAndrew, supra n.117.

in the face of the two House of Lords' decisions to the contrary. In *Heyman* v. *Darwins*[120] and *Hain Steamship* v. *Tate & Lyle*[121] it was explained that only a right to repudiate was given to the aggrieved party and that right can even be lost by waiver. The tendency has consequently been to regard the deviation cases as a special class of their own.

The idea of displacement, which was in a sense a cryptic but erroneous representation of the Gibaud rule, contributed little to the understanding of the rationale and effect of the rule. It rather succeeded in confounding it. In *Woolf* v. *Collis Removal Service*,[122] for example, it was insisted that deviation was a form of repudiation which could be accepted or rejected by the aggrieved party whereupon an exception clause applied according to its ambit. But as Lord Atkin intimated in *The Cap Palos*,[123] the Gibaud rule regulated the manner in which one performs his contractual obligations by compelling him to observe a basic degree of compliance with the terms of his promise. Consequently if he failed to do so he would not be allowed to rely on an exception clause, even if the aggrieved party insisted that the other had fulfilled his obligations. In such instances, said Lord Atkin, it was not a question of the repudiation of a contract to be accepted by the other party in order to give rise to a claim for breach.[124]

Although deviation did not by definition include, for instance, delay[125] or unseaworthiness,[126] its consequences applied to analogous situations even in contracts other than contracts for carriage of goods by sea. Thus in contracts for the carriage of goods on land, a performer would have stepped outside the 'four corners' of his contract where the voyage was abandoned or where there was such unreasonable delay as to constitute a "fundamental departure" from the course of the agreed transit,[127] or where carriage was in a vehicle other than that stipulated for,[128] or where carriage was to a wrong destination.[129]

120 [1942] A C 356.
121 [1936] 2 All E.R 597 at 603, 607-608, 615
122 [1947] 1 K.B. 11, the decision here, however, turned on the fact that an arbitration and not an exception clause was in question
123 [1921] P 458 (C A)
124 Id at 471
125. The Monarch [1949] A.C. 196 (H.L.)
126 The Europa [1908] P. 84 (C.A.), Kish v Taylor [1912] A C. 604 (H.L).
127. Per Lord Sumner in Cunard Steamship v Buerger [1927] A C 1 at 8; Bontex Knitting Works v St Johns Garage [1943] 2 All E.R. 690.
128 Sleat v. Fagg (1822) 5 B. & Ald. 341, 106 E R. 1216; Garnett v Willan (1821) 5 B & Ald. 53, 106 E.R 1113, Gunyon v S E.C Railway [1915] 2 K.B 370
129 L & N W Railway v Neilson [1922] 2 A C 263 (H.L).

(b) Contracts of Storage and Deposit

The essence of the contract by a warehouseman, it has been explained, is that he will store the goods in the contractual place and deliver them on demand to the bailor or to his order.[130] Thus the wrongful or mistaken sale of the bailed goods,[131] their consumption,[132] their delivery without excuse to the wrong person,[133] their storage in a place other than agreed upon,[134] or the permission of access to them by unauthorised third parties[135] are all acts outside the 'four corners' of the contract. But the warehouseman who has observed these duties may be protected by an exception clause even though in one case, when delivered, five out of the eight casks of orange juice left in storage were empty without lids, two were leaking badly and one had dirty water in it.[136]

However, it does not follow in every case that the observance of these duties always ensures the bailee of the protection of an exception clause, for they must be carried out with reasonable care. While "mere negligence" or some "momentary piece of inadvertance"[137] in carrying out the contract may not deprive the bailee of the protection of the exception clause, recklessness may amount to stepping outside the 'four corners'. The reason is that a performer "cannot be allowed to escape from his obligation by saying to himself 'I am not going to trouble about these goods because I am covered by an exempting clause' ".[138] Thus "all these exempting clauses are held nowadays to be subject to the overriding proviso that they avail to exempt a party only when he is carrying out his contract."[139]

Where a bailee divests himself of his charge of the goods or does anything inconsistent with the title of the owners, the risks of such misperformance cannot be passed to the bailor. Here the quality of his conduct or state of mind is immaterial. For such a misperformance is a complete contradiction of the purpose of the contract. But short of such an inconsistent misperformance, it seems that the risks of outright defiance of an

130 Spurling v Bradshaw [1956] 2 All E R. 121.
131 Woolmer v Delmer Price [1955] 1 Q B. 291 at 295; Spurling v. Bradshaw [1956] 2 All E.R. 121
132 Spurling v Bradshaw [1956] 2 All E.R 121
133. Alexander v. Railway Executive [1951] 2 K.B 822.
134 Lilley v Doubleday (1881) 7 Q.B D. 510, Edwards v Newland [1950] 1 All E.R 1072
135. Alexander v Railway Executive [1951] 2 K B 822
136. Spurling v. Bradshaw [1956] 2 All E.R 121
137 In Hartstoke Fruiterers v L M.S Ry [1943] 1 All E.R 470 the carrier negligently failed to inform the consignee in accordance with the contract of the arrival of bananas with the result that they were seriously spoilt by the climate. The relevant provision was said to be a "merely ancillary provision not bearing upon the contract of carriage at all", at 472; cf. Sze Hai Tong Bank v Rambler Cycle [1959] A.C. 576 (P C.); Wedderburn, 'Contracts — Exception Clauses — Fundamental Breach — Agents' (1960) 18 *Camb L J* 11
138 Spurling v. Bradshaw [1956] 2 All E.R. 121, at 125
139. Id. at 124.

acknowledged duty (for example, in *Sze Hai Tong Bank* v. *Rambler Cycle*) cannot be imposed on the bailor.[140] Risks of recklessness and indifference to the safety of the goods bailed also warrant similar treatment.[141] Risks of negligence are more difficult.[142] On the one hand although it was thought that negligent destruction of property warehoused is not sufficiently serious, it was not suggested "that negligence can never go to the root of the contract".[143] On the other hand it was hinted in *Hollins* v. *Davy* that an honest error may be excluded: "where a person is when doing an act honestly intending to do his best to carry out the intent of the contract and that act is one which, if his beliefs were true, would be proper under the contract, he cannot, merely because he has been deceived into the action, be said to be deliberately breaking the contract in question". Therefore if in the same contract for the bailment of a care, the bailee by an honest mistake sells the vehicle or sends if off to the breaker's yard he will be liable notwith-standing an exception clause which *prima facie* protects him.[141] Contrary views are held on a negligent misdelivery. In *Alexander* v. *Railway Executive* and *Sze Hai Tong Bank* v. *Rambler Cycle* it was suggested that risks of a misdelivery with the knowledge that it is to the wrong person or in an unauthorised manner may not be passed to the bailor. However, it was said earlier that a mistaken misdelivery of goods to the wrong person, however innocent, was a conversion.[145] "Property rights are protected at the expense of an innocent mistake".

(c) Contracts of Towage

The failure to exercise care and skill may well be the primary if not the only means by which a performer may be found to have stepped outside the 'four corners' of his contract. The quality of the misperformance is the paramount consideration. Thus in *The Cap Palos*[146] the performer's misperformances were differentiated qualitatively.

140 In Hollins v. Davy, Sachs J. held that a breach must be wilful or deliberate in order to constitute a fundamental breach [1963] 1 Q.B. 844, Lord Denning's dictum in Sze Hai Tong Bank v. Rambler Cycle [1959] 3 All E.R. 182 (P.C.) and Sir Wilfred Greene M.R.'s dictum in Ashby v. Tolhurst [1937] 2 K.B. 242 (C.A.) relied on.

141. Spurling v. Bradshaw [1956] 2 All E.R. 121 (C.A.); Colverd v. Anglo-Overseas Transport [1961] 2 Ll.L.R 352; John Carter v. Hanson Haulage [1965] 1 All E.R. 113; Gillette Industries v. Martin [1966] 1 Ll.L.R. 57.

142. See the discerning discussion by Guest, in 'Fundamental Breach of Contract' (1961) 77 *L Q R* 98, 114-115, of whether negligence can amount to a fundamental breach. It anticipates many of the points discussed here. Guest's analysis, however, only seeks to identify the different incidences of fundamental breach in the cases and does not explain fundamental breach on a theoretical basis. See also Clarke, 'Fundamental Breach of Charter-Party' [1973] *Ll 's M C.L Q* 472.

143. Spurling v. Bradshaw [1956] 2 All E.R. 121 (C.A.).

144. 'Negligence and Fundamental Breach' (1963) 26 *Modern L Rev.*, 301.

145. Devereux v. Barclay (1819) 2 B. & Ald. 702, 106 E R. 531.

146. [1921] P. 458 (C.A.).

There, the use of insufficient towage power or possibly the improper use of sufficient towage power by the defendants had resulted in the grounding of the plaintiff's schooner in a dangerous area. The defendant's negligence in not making allowance for changes of wind and other considerations which resulted in the grounding of the schooner did not amount to stepping outside the 'four corners' of the contract. This negligence was perhaps regarded as an inadvertent oversight or an excusable exercise of poor judgment. The defendant could consequently invoke and was protected by the exception clause. The negligence, it was said, happened in the course of the actual performance of the contractual duties.

However, the unjustified failure to send assistance to get the schooner to a place of safety and the "unjustified handing over of those obligations to [the Salvage Association] for performance" were defaults to which the exception clause whatever its ambit did not apply.[147] This was so despite the fact that the defendants had received intimations from the insurance underwriters to the effect that the Salvage Association had dispatched tugs to rescue the schooner and that it usually ended up taking charge of a rescue operation without the help of anyone who may have a towage contract with the shipowner. Lord Sterndale M.R. suggested that many things could still happen; the Association's tugs might not arrive, as indeed they did not here, and the defendants ought not to take that risk but should have sent their tugs to the schooner's rescue. Their failure to exercise "reasonable industry" to rescue the schooner from the danger in which they by their own breach had put it was considered analogous to the hypothetical example of their casting off the tow in a storm on a lee shore for the purpose of engaging in a more profitable salvage operation and the tow in consequence being damaged.

What qualities of negligent conduct would be acceptable subjects of exclusion is not quite clear, but in *The Albion*[148] the court saw fit to caution against the relaxation of the 'four corners' requirement to include situations of non-compliance with contract terms that do not significantly increase or alter the nature of the risks borne by the aggrieved party in the normal course of events as contemplated under the contract. It was feared that "the words 'fundamental breach' might be read in this

147. Id. at 468, per Lord Sterndale M R
148. [1953] 1 W.L.R. 1026 (C.A.).

context in a wider sense than the decisions justify".[149] In *Bontex Knitting Works* v. *St. John's Garage*[150] for instance, a delay of an hour in a contract of carriage for two and a half hours deprived the carrier of the exception clause. There Lewis J. spoke only of the delay as a breach of contract, paid little attention to when one would have crossed the imaginary demarcation and thus suggested, perhaps, a wider application of the rule.

(d) Contracts of Laundering

In these contracts, launderers "undertake, not to exercise due care in laundering the customer's goods, but to launder them, and if they fail to launder them it is no use their saying, 'We did our best, we exercised due care and took reasonable precautions, and we are very sorry if as a result the linen is not properly laundered'."[151] Reasonable industry therefore is not the only relevant consideration in deciding whether a launderer has basically complied with the terms of his promise. Here the spatial dimension of the 'four corners' of a contract is not at all visible and the criterion becomes translated into the "primary obligation" to launder. It is now described as the "hard core of the contract, the real thing to which the contract is directed", and the "essence of the contract". Consequently the essential service of laundering cannot be sub-contracted without the consent of the customer although, in contrast, an "ancillary service" such as sending the goods back to the customer by post may if necessary be sub-contracted.[152] Similarly the launderer's duty of performance in respect of ancillary tasks is only to act with reasonable care.

In effect, the Gibaud rule introduces into these service contracts a minimum standard of compliance with contract terms to ensure that a performer observes a basic duty of performance of his obligations. This minimum standard is figuratively represented as the 'four corners' of the contract. An exception clause will be overriden, however wide its ambit may be, if the performer 'steps outside' the 'four corners'. In other words, a performer is to this extent prevented from unilaterally increasing supervening risks of misperformance, including risks of the performer's breach, which the other party otherwise bears in the normal course of

149 Id. at 1031; see Colverd v Anglo-Overseas Transport [1961] 2 Ll L R 352, which Wedderburn regards as a "useful corrective" against overemphasising the effect of cases like Bontex Knitting Works v. St Johns Garage, 'Fundamental Breach of Contract – Onus of Proof' (1962) 20 *Camb L J* , 17 at 18 In Colverd's case the negligence of one of the carriers' drivers in leaving the garage door unlocked resulting in the theft of a batch of watches from one of the lorries stored in the usual manner in the garage was held to be only an "isolated lapse" on the part of the driver which did not go to the root of the contract

150 [1943] 2 All E R 690.

151 Alderslade v Hendon Laundry [1945] 1 K B 189 at 193 per Lord Greene M R

152. Davies v. Collins [1945] 1 All E R 247, at 251, Alderslade v Hendon Laundry [1945] 1 K B 189 at 193.

events. For the area and the chances in which that loss may occur are indefinitely increased when the performer does not comply with the contract terms when he attempts to perform.[153] A performer, therefore, cannot expressly excuse himself in advance from liability for breach and then not trouble himself with the manner in which he seeks to render performance of his contractual obligations since the other party will not be made to bear the brunt of any increased risk arising from outside the 'four corners'.

Negligent Misperformance : Recent Developments

There seems to lurk behind tentative judicial observations an intuitive conception of different qualities of negligent conduct, so that between wilful default on the one hand and honest mistake on the other, there may be a scale of culpability. This would mean that the prevailing general notion of negligence is now recognised as encompassing a whole spectrum of modes of culpability which need to be distinguished and dealt with accordingly. What is until now undiscriminatingly regarded as negligence may be, for example remissness, oversight, lack of circumspection, indifference to avoidable risks, conscious disregard of known risks, carelessness or intentional misconduct or default.

A review of the three cases — *Harbutt's Plasticine*,[154] *Kenyon* v. *Baxter Hoare*,[155] and *Photo Production* v. *Securicor Transport*[156] — reveals a subtle and consistent pattern of regulating negligent misperformances. We shall now attempt to extrapolate the coherent structure of results from them.

In *Harbutt's Plasticine* the mistakes made by D were blatant and elementary evincing appalling incompetence on their part. As the court of first instance found as a matter of fact, it was a "major blunder" for D to use durapipe at all. Stearine remains in a molten state at a temperature between 120F and 160F while durapipe distorts at 187F. The "margin of safety" between the two was thus "dangerously small". Furthermore because of the low thermal conductivity of the durapipe it was by no means clear that an internal temperature of 160F could be attained without ex-

153 Lord Wright in Rendall v Arcos (1937) 43 Com Cas 1, at 15 delivered the opinion of the House of Lords in these words. "The essence of the principle is that damage has been sustained under conditions involving danger other than and therefore different from the conditions which would have operated if the contract had been fulfilled, for the consequences of such conditions the defendant is held liable. The principle thus applies whenever the breach of contract has the consequence of exposing the subject-matter to conditions of risk different from those which would have operated if the contract had not been broken . The defendant must show (if he can) that there must have been the same damage if the contract had not been broken the mere fact that the risk is changed will be enough to shift the onus on to the defendant"

154 [1970] 1 All E R 225

155 [1971] 2 All E R 708

156 [1980] 2 W L R 283 (H L)

ceeding an external temperature of 187F. The low thermal conductivity of the durapipe also made it difficult to maintain a constant temperature along the length of the pipe and rendered a thermostat useless. For it could provide no reliable indication of the varying temperatures at different parts of the durapipe: a spot underneath the electric heating tape would register a temperature much higher than one away from the tape. "In the result it was inevitable that, if the tape was energised, the exterior of the pipe in contact with the tape would become dangerously hot before the interior of the pipe reached 160F, and that in the absence of an effective thermostat the external temperature might build up until the pipe disintegrated and the now highly inflammable stearine came into contact with the heating element in the tape"[157]. D had "designed, supplied and erected a system which was thoroughly . . . *wholly* — unsuitable for its purpose . . ., and certain to result not only in its own destruction but in considerable further destruction and damage . . ."[158].

The risks that arose from the breach were risks of experimentation only in the sense that durapipe was used by D for the first time. They were not risks of experimentation in the true sense which would arise if for instance the properties of durapipe were uncertain and the parties had nonetheless agreed to test its use in the installation. The risks inherent in the innovation and arising from the uncertain (hence unavoidable) would be true risks of experimentation. These latter risks may arguably be passed to the payor[159]. In the instant case the risks arose indisputably from D's incompetence. The regrettable mistakes stemmed from D's failure to consider the law thermal conductivity of the durapipe. The unsuitability of the durapipe was so basic that its use together with the fact that D were experts in conveying liquids could only be regarded as incompetence and negligence of the gravest kind. So that even if it was P who had preferred the durapipe on account of some small reduction in cost, D, by reason at least of their special skills vis-a-vis P, had a duty to advise P that it was unsuitable. This as Widgery L.J said, D had not done because "no thought" was given to it[160]. Moreover, D "ought to

157 [1970] 1 All E R 225 (C.A.) at 237 per Widgery J.

158. Id. at 231 per Lord Denning M.R. quoting the finding of the trial judge.

159 In his article 'More Exemptions, Not Less' [1967] *J Bus.L* 133, Johnston voiced a widespread concern that legitimate exception clauses in commercial contracts may be unjustifiably disallowed by fundamental breach as a rule of law He gave the example in which company A buys from company B and instals an electronic system for some novel purpose. Numerous different pieces of equipment, possibly situated in different parts of the country, all of which must work together are involved. The pieces of equipment may be tested separately but there is no means of testing the whole system short of installing it completely and operating it. If the system fails A loses the whole benefit of the contract and B is, he fears, by any means in fundamental breach of his contract. But according to our analysis, B may well be protected by an exception clause, the performance-related risks being, unlike those in the Harbutt's Plasticine case, risks similar to true risks of experimentation.

have known" that leaving the tapes energised and unattended was liable to cause the collapse of the durapipe and was a "dangerous risk of fire". Indeed if the installation was experimental, as D claimed, this negligence on their part (and conceded by them) may well be regarded as recklessness[161].

Kenyon v. *Baxter Hoare* is more difficult to explain. The warehousemen's "gross and culpable"[162] failure to use reasonable care and skill seems on the face of it only a shade different, if at all, from the incompetence of D in the *Harbutt's Plasticine case.* Theirs, as the court said, was "not deliberate and conscious neglect or default"[163]; theirs was the "carelessness of the fatalist and defeatist" a "carelessness of the incompetent" but "not a reckless carelessness".

It is of course possible to distinguish the two cases on the ground that in *Kenyon* v. *Baxter Hoare* the misperformance seems to be only in respect of a minor portion of the nuts and did not give rise to consequences of a comparable magnitude. But this would not be entirely satisfactory, for the suggestion is that apart from the consequences of the breach the quality of the misperformance is also material. Perhaps a better explanation is this. When rats infest nuts warehoused in a locality where rats are known to be common, such an occurrence is not too unlike a natural disaster, the consequences of which one can too easily not completely foresee. The natural attraction of high protein food for rats makes the task of preserving and storing the nuts more difficult even for experienced warehousemen. The negligence in question arose from the "dim lights" according to which the warehousemen looked after the nuts, and the "wholly mistaken, but sincerely held belief" that what they did was all that they may be expected to do. The risks of this remissness or unawareness of the risks involved may be acceptably passed to the owners of the goods. This is arguably the case even if the damage was decidedly substantial.

How then can Securicor in *Photo Production* v. *Securicor Transport* justifiably shift the risks of its employee's negligent misperformance which results in the substantial destruction of the factory to the owners? Ordinarily, where the contract is actually performed by persons other than the contracting party the law implies an absolute responsibility on the part of the contractor for his employee's exercise of reasonable care and skill. But if the employer has taken due care to delegate and supervise

160. [1970] 1 All E.R. 225 (C.A) at 237.
161. D unsuccessfully sued their insurers: Wayne Tank & Pump v. Employers' Liability Assurance Corp. [1947] 1 Q.B. 57.
162. [1971] 2 All E.R. 708 at 716.
163. Id. at 717.

performance to a particular employee, the former may pass risks of the employee's misperformances which he cannot control by reasonable diligence to the other party. Here what Securicor seeks to guard against are risks of fire which can be said to arise from acts or events which are not only extraneous (and therefore cannot be prevented) but also against the consequences of which the owners of the factory had already protected themselves by insurance. This was perhaps the idea that lurked behind Lord Wilberforce's warning that it is "important to bear in mind" that the employee did not intend to destroy the factory although he deliberately lit the fire. Underlying this caution seems to be a hint that if the employee had intended to destroy the factory, Securicor would not have been able to pass the risk of such deliberate or intentional misperformance to the owners even though they exercised due care in the supervision of their employee's conduct. This in turn suggests that our explanation should not be put too widely. Any exclusion of liability for the consequences of specific things done by Securicor's employees, say pilfering, would (in the same way as arson) be quite distinguishable on the ground that the employee would be doing precisely what Securicor was not supposed to do thereby bringing about the very risk which it was supposed to guard against.

It will be oversimplifying matters as well as misleading to say that the element of consistency in the three cases is to be found in the risk of negligent misperformance, a risk we find in each case. For such risks of negligent misperformance that may be passed to the payor, in spite of the destruction of the substratum, entail elements which are immensely difficult to avoid and hence are in a sense comparable to extraneous circumstances. But these analogous extraneous circumstances are to be distinguished from the extraneous circumstances that have often given rise to dispute in yet another group of service contracts. They are the irresistible forces that commonly cause damage in charterparties where a ship is deviating from its course but the risks of which cannot by virtue of the Gibaud rule be passed to the payor. The different treatment of the two types of extraneous circumstances is warranted by the fact that in the first type of service contracts the analogous extraneous circumstances are not brought on or induced by avoidable deliberate conduct. Whereas in the second group of service contracts, the risks of the extraneous circumstances arise because the performer by his own avoidable conduct deliberately subjects the payor to them.

Wilful Misperformance

Apart from risks of negligent misperformance, there is a more specific

type of performance-related risks of which *Suisse Atlantique* is an excellent example: the risks of wilful misperformance calculated to and which did in fact diminish the aggrieved party's profitability under the contract by half. Unfortunately the House of Lords then did not quite grasp the question posed[164] or appreciate the significance of the facts.

It will be recalled that under a two-year consecutive voyage charter for carriage periods of laytime were fixed within which the charterers were to load and discharge the vessel. Demurrage was payable at an agreed rate for delay in loading and discharging while compensation was payable for earlier discharge or loading. As a result of delays by the charterers in loading and discharging beyond the laytime the number of voyages that could be made if the loading and discharging had been within the laytime was reduced. It was suggested that the subsequent fall in market freight to below the charter freight or the diminished profitability of the charterers' coal trade accounted for the charterers' deliberate delay in loading and discharging for every voyage performed other than the first. The owners' case therefore was that as a result of the charterers' wilful intention to limit the number of voyages the venture was made so much less profitable to them by the loss of voyages that the charterparty was fundamentally breached and they, the owners, were entitled to damages for the loss apart from any demurrage. The owners claimed that they were entitled to a minimum number of voyages compatible with compliance with the laytime. By their calculation six more voyages than the eight made by the end of the two years could have been completed if the charterers had loaded and discharged within the laydays stipulated or a further nine if they had loaded and discharged the vessel with reasonable dispatch. The loss of cargo or freight in these circumstances, the argument continues, was not and was not intended to be compensated for under the demurrage clause. For the demurrage clause was only concerned with delay in loading and discharging. In other words, the owners' case was that they had not assumed all the performance-related risks of the charterers' delay howsoever caused and however excessive and were protected from the risks of the charterers deliberately making a "startling difference" to the profits of the charterparty. From the charterers' point of view this amounted to a contention that they must be made to observe certain standards of performance which at the least precluded them from deliberately causing the owners to lose freight by the kind of delay in question. Alternatively, the owners argued, in a consecutive voyage charter the charterers had contractual rights to compel

164 Fraud and bad faith were only mentioned cursorily and not particularly in the context of a deliberate (wilful) misperformance of about half the consideration The distinction between bad faith and the wilful default in question was also hazy

them to carry further cargoes under the charterparty and they had corresponding rights, there being an express or implied obligation of the charterer to allow a plurality of voyages. Hence the claim was not for breach of the laytime provision simpliciter but for the breach of a separate obligation derived from the charterparty as a whole to permit the owners to load on the number of voyages performable given compliance with the laytime.

In *Suisse Atlantique* the charterers ought not be protected by the demurrage clause. The delay was indisputably contrived to defeat the shipowner's venture: the charterer had only loaded and discharged the ship for the first voyage within the laytime. Delay for the rest of the voyages was systematically calculated virtually to enable the charterer to escape the full rigours of a contract, which because of subsequent extraneous events turns out to be unfavourable to them. Besides, a demurrage clause is not an ordinary exception clause but is an agreed damages clause not unlike the common penalty clause in building contracts. In including such clauses, parties to a contract anticipate that contingencies may arise which hamper performance of the contract and agree to a pre-estimation of the damages or compensation that each will get. The demurrage clause is certainly concerned with the more usual kinds of delay that may occur. For instance, the charterers may not be able to load within the laytime because of strikes by their employees or by persons from other quarters which affect the general business of loading and unloading. Perhaps even a purposeful delay may be contemplated. But if the charterers delay loading and unloading in order to reduce the number of voyages otherwise possible within the two years so that they, the charterers, will not have to pay the charterparty freight which, as a result of a subsequent drop in the market freight, renders their bargain a bad one, the demurrage clause cannot be said to provide for it. What the charterers do here is not dissimilar to the example given of the performer in the *The Cap Palos* who abandons the boat, which he has contracted to tow, on a lee shore in order to pursue a more profitable engagement with another party. The charterers in *Suisse Atlantique* are effectively licensed to use the demurrage clause to remedy a bad bargain by actively and wilfully forcing the shipowners to bear the loss of their calculated misperformance. Thus if the performer in *The Cap Palos* could not shift the risks of his negligent misperformance, which led to the destruction of the schooner, to the other party then *a fortiori*, the shipowner here ought not to be regarded as having assumed the risks of the charterer's wilful misperformance which was by no means of minor consequence.

Conclusion

If it is necessary to put the intuitive differentiation of performance-related risks on a more general basis, it may be said that it turns on the quality of the breach and the consequences of breach. All performance-related risks, unlike risks arising from unforeseen supervening events, are risks arising from culpable (in the sense of avoidable) misperformances. A performer cannot unilaterally impose upon the payor increased risks of certain kinds of culpable misperformance which result in a total collapse of a bargain[165].

Generally when a bargain collapses totally in consequence of a breach, an aggrieved party is entitled to be discharged of his obligations under the contract irrespective of any exception clause that may provide to the contrary. The reason is that in every bilateral contract, apart from contracts of chance, there is a minimum standard of exchange which cannot be eviscerated or emptied and for the non-performance of which the aggrieved party should not have to pay. For otherwise a performer would be allowed to subject the other party to what is at best a different contract without entitling the latter to rescind on account of the exception clause. The minimum standard of exchange thus preserves the essential bargain. And in every case the question is whether a party has received that minimum degree of performance of the particular exchange expected under the contract.[166]

Generally, too, whether all other exception clauses which directly or indirectly modify the payor's usual remedy in damages apply, where a bargain has collapsed totally, depend on the type of performance-related risk involved. This in turn depends on the quality of the breach and the nature of the contractual obligation. Where the breach is wilful the performer is not protected whatever his obligation may be. Otherwise his promise amounts in effect to a potestative condition.

The idea that risks are differentiated according to the quality of conduct introduces into the law a distinction between culpable and innocent breach which may have a wider significance. Traditionally a breach is said to be committed when a party "without lawful excuse, refuses or fails to perform, performs defectively or incapacitates himself from performing the contract"[167]. But according to our idea that risks are differen-

165 Cf. the Louisiana Civil Code in which there are more sophisticated provisions that recognise at least three degrees of fault, namely, gross, slight and very slight fault. The relations between them and the extent of liability are also clearly established; see Litvinoff, 'Stipulations as to Liability and as to Damages' (1978) 52 *Tulane L Rev* 258; see also Rieder, 'Exculpatory Clauses' (1975) 36 *Alabama Lawyer* 254; Tillman, 'Restrictions on Attempts to Contract Away Liability for Negligence' (1960) 12 *Baylor L Rev.* 298.

166. 'The Treatment of Breach of Contract' (1966) 24 *Camb L J* , 192.

167 G.H. Treitel, *Law of Contracts* 4th ed. (1975) at 571.

tiated according to the quality of conduct, a breach may be innocent where a party fails to give what he is supposed to give without intending to refuse or to repudiate performance. A ready example is where a party fails to perform because of an unexpected financial difficulty which forces him out of business[168]

Apart from enabling courts to determine who should bear the risks of different kinds of culpable breach, such a distinction between culpable and innocent breach can also form the basis for protecting a performer's reliance and restitution interests. So that where a performer has incurred loss in preparing for the performance of his promise in reliance on the contract, the other party can be made to share the loss on the basis that the former's breach was innocent.[169]

The law on part performance which gives rise to unsatisfactory questions of unjust enrichment may be profitably re-structured on a similar basis. An argument of Treitel's supports the latter idea and by a parity of reasoning, supports the former as well. He contends that the Law Reform (Frustrated Contracts) Act 1943, which protects the performer's restitutionary interest to some degree, should be extended and applied to make some form of restitutionary relief available even where the failure is due to breach. The distinction between frustration and breach, he said, is "not so firmly based on moral considerations as to justify the imposition of what is in substance a penalty in the latter case".[170] Thus it was hard to see why a builder disabled by a credit squeeze should be more harshly treated than one disabled by supervening illegality. The current general proposition that performance of every entire contract must be complete penalises performance: where performance is incomplete the innocent party gets something for nothing and the performer is prejudiced. Indeed the less serious the defect the greater is the penalty. Foreseeably the main relevance of this protection will not be in situations of severe breaches where in most, if not all, cases no benefit as expected under the contract is conferred because the bargain collapses totally.[171]

168 Sumpter v Hedges [1898] 1 Q B. 673.

169 A parallel development already exists in frustration where s 1(2) of the Law Reform (Frustrated Contracts) Act 1943 extends limited protection to the performer who incurs detriment in reliance on a contract which is subsequently frustrated. See generally G.L. Williams, *Law Reform (Frustrated Contracts) Act 1943* (1944).

170. Treitel, 'Some Probelms of Breach of Contract' (1967) 30 *Modern L Rev* , 139 at 143 He suggests an approach based on more practical considerations rather than the extensive conceptualisms and metaphors that riddle the law. The problem has to be looked at from these planes: (i) the distinct nature of the problems of defective performance, (ii) the practical effects of possible remedies and (iii) the respective interests of the parties in using or resisting the use of any remedy Contra Lord Devlin 'The Treatment of Breach of Contract' (1966) 24 *Camb L J* 192 who seems to prefer a more conceptual approach.

171 The exception may be the cases involving a failure to pass title in goods typified by Rowland v. Divall [1923] 2 K.B. 500.

A final word may be said here about the very strict view taken of deviation. The exceedingly heavy burden of proving that had it not been for the deviation the same loss would still have occurred[172] is now, it is submitted, due for revision. The consequences flowing from the deviation should also be taken into account. The compelling historical and commercial reasons in the days when the hazards of the sea were far more forbidding than what they are today would have lost much of their relevance. And as Lord Devlin argues:

> It may be that when a man is in breach of contract you can justifiably put a heavy burden of proof on him to show that his fault did not materially contribute to the disaster but you need not put upon him the almost impossible burden of showing that if there had been no fault, the goods would inevitably have been destroyed . . .[173]

172 Negligent navigation is not deviation: Rio Tinto v Seed Shipping (1926) 42 T L.R 381, even where the ship was wrecked as a result.

173 'The Treatment of Breach of Contract' (1966) 24 *Camb L J* 192 at 202. It would, he says, be sensible too to have an apportionment here according to the part played by each.