Koffman & Macdonald's

Law of Contract

Eighth Edition

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Chapter 1

Introduction to the study of contract law

What is a contract?

1.1 A contract is a legally enforceable agreement giving rise to obligations for the parties involved. The law of contract determines which agreements are enforceable and regulates those agreements, providing remedies if contractual obligations (undertakings or promises) are broken. Under a contract, the parties voluntarily assume certain obligations or undertakings: for example, S promises to supply a new car to B by the end of the month, whilst B promises to pay, on delivery, the price of the vehicle. Their agreement to perform these undertakings is a contract. There is no legal duty to enter into such an agreement, but if the parties choose to do so, it will give rise to legal obligations. Therefore, the law of contract is distinct from branches of law where duties are imposed: for example, there is a general duty (in the law of tort) to take care that we do not injure other people by our careless actions. The doctor whose treatment of a patient falls below the professional standard expected of an ordinary practitioner of medicine may be liable for negligence. This liability is not based on a contract (indeed, there is no contractual relationship between a general practitioner and a National Health Service patient); it is a general duty of care imposed by law.

1.2 The word 'contract' suggests to most people a formal or technical document drawn up and understood only by lawyers. Contracts can take this form, and certain types of contract (for instance, for the sale of land or any interest in land) must be in writing; but generally a contract can be made orally, without any legal jargon or formality. We all make numerous contracts as part of everyday life and we rarely give thought to legal technicalities. Making a contract is simply a way of facilitating, amongst other things, the exchange of goods and services. It is merely a method of commercial transaction. Of course, the transaction can vary enormously in complexity and in value—from the purchase of a chocolate bar to the multi-million pound takeover of a large company—but it is based on a contract nevertheless.

1.3 To illustrate the importance of contracts in our society, let us consider a day in the life of a fairly ordinary person (X), from the point of view of his contractual relationships. In the morning, the milkman delivers two pints to X's house and X buys a newspaper on the way to work. Both transactions are contracts for the sale of goods. X goes to work on the train, riding under a contract of carriage, and performs various tasks at work under a contract of employment. Later, X returns to a house which is probably subject to a very important contract, namely a lease or a mortgage. X is having the house redecorated, under a contract for the provision of services and materials. X takes a ride in the car that X is buying under a hire purchase agreement, and which is protected by a contract of insurance. On returning home, X watches a DVD which is hired from a local shop. Finally, X walks the dog—no contract there!

The law of contract/s

1.4 There are particular types of contract, such as contracts of employment and contracts for the sale of land, which are subject to their own specialized rules of law and detailed legislation. The law of contract, however, has long survived as such, and is the study of the legal principles which underlie all contracts. It is not (generally) concerned with particular types of contracts and their specialized rules, but provides the important foundation for these specific areas.

1.5 The law of contract is a common law subject: it is primarily derived from the decisions of the courts (precedent), and these judicial rulings constitute the relevant law. Many principles of contract law owe their existence to decisions dating back hundreds of years, whilst some are of comparatively recent origin.

1.6 There are, of course, some important statutes in the general law of contract, for example the Law Reform (Frustrated Contracts) Act 1943, the Misrepresentation Act 1967, the Contracts (Rights of Third Parties) Act 1999, and the Unfair Contract Terms Act 1977. However, there is an increasing volume of consumer contract legislation. In the consumer context, the Unfair Terms in Consumer Contracts Directive has a far broader reach than the Unfair Contract Terms Act 1977. The Law Commissions have taken the view that consumers need clearer, simpler, and more effective, rights in relation to misleading and aggressive trade practices than is provided by the general contract law on duress and misrepresentation,[1] and the draft Consumer Protection from Unfair Trading (Amendment) Regulations would bring that about. Such an increasing volume of broad consumer legislation may start to create a much more significant division of contract law, than anything which has previously occurred, into commercial, and consumer, contract law.

1.7 Although contract is common law subject, a study of appeal court decisions can create the misleading impression that contracts lead inevitably to disputes and conflict. A contract

1 The Law Commissions, *Consumer Redress for Misleading and Aggressive Practices* (Law Com No 332, Scot Law Com No 226) para. S.18.

law book or course deals with what are comparatively rare (namely legal action in the courts). Traditional approaches tell us little about business practice and how it differs from the formal law. It is particularly important in the area of contractual remedies that we do not overemphasize the importance of lawyers and the courts. As we have noted, a contract is simply a means of facilitating exchange (of goods, services, etc.) and if there is a dispute over its interpretation, or even if one party clearly breaks the agreement, this does not inevitably lead to litigation and the courts. The costs of a legal action can be prohibitive and only the very wealthy can contemplate protracted litigation without considerable unease.

1.8 Even where the parties can afford to go to court there may be good reasons to try to avoid doing so. In commercial practice, some breaches of contract are seen less as a legal problem and more as a commercial one. Companies will want to avoid any damage to their reputation that might be caused by litigation. A legal action with its formal style, its conflict approach, and its demands on time and money, can be damaging to continuing relationships in the business world. Even if successful, a party will normally fail to recover all the expenses that were incurred. For these and other reasons, business people try to resolve disputes without recourse to the courts. The same also applies to the consumer who, generally, can ill afford to take a claim to law. It is better to try negotiation and persuasion in the event of a contractual dispute.

'Freedom of contract'/Inequality of bargaining power

1.9 Many important contractual principles, as expounded by the leading decisions of the courts, were established in the eighteenth and nineteenth centuries. The 'classical' view of contract was that the parties entered into an agreement or bargain freely, and therefore there should be as little state regulation or intervention as possible. It was not the task of the law to ensure that a fair bargain had been struck. This attitude was consistent with the laissez-faire philosophy which was so influential in the thinking of the time; it was consistent with the idea that contracts should be made by the parties (with freedom of choice) and not be imposed on them by the state. It was thought to be consonant with a free market economy and the spirit of competition.

1.10 Even in its historical context, this approach raises obvious questions. It assumes a particular model of contractual activity: namely that between business people of fairly equal resources. It assumes the existence of genuine competition. Of course there never was true equality—a prerequisite for freedom of contract. How could such a doctrine apply as between employer and employee, for example? In a more modern context, such a laissez-faire 'world-view' seems absurd. It fails to take account of groups who are particularly susceptible to exploitation, such as consumers, tenants, and employees.

1.11 However, the important concept of inequality of bargaining power came to be recognized. A major influence in the decline of the freedom of contract philosophy was the emergence of the consumer as a contractual force. The traditional model of contracts as a means of exchange between business people had to accommodate the idea of exchange between a business person

and a consumer. Inevitably inequality of bargaining strength (in relation to wealth, resources, and experience) had to be acknowledged. The twentieth century saw a move towards greater state regulation of many types of contract. A good example is the Unfair Contract Terms Act 1977, which went further in regulating and restricting the use of exclusion clauses than any previous control provided by the courts. There is also public law regulation of consumer affairs and the increasing influence of European directives.

1.12 There is acceptance of the idea that certain contracting parties need the protection of the law against economic exploitation and oppression. Major legislation has gradually helped to prevent the exploitation of tenants and employees and to reduce the incidence of gender discrimination. However, the extent of protection which is needed and the extent of the departure from freedom of contract, which should occur, is still hotly disputed. The law of contract is often engaged in trying to balance traditional market liberalism with the need to protect those who may be exploited. As we shall see, one of the most recent contexts in which the battle between the opposing forces of market-liberalism and consumer-welfarism has been fiercely fought is in relation to the scope of the legislation derived from the Unfair Terms in Consumer Contracts Directive.

Europe

1.13 The European Union has had significant impact upon English contract law. It has brought about significant legislation, such as that implementing the Unfair Terms in Consumer Contracts Directive. It has also simply made English lawyers more aware of the law of other European states, which has particularly occurred through projects like the drafting of the *Principles of EU Contract Law*,[2] produced by a group of academic lawyers from different member states. Such awareness brings consideration of alternative legal strategies which might be adopted by English law. However, there has also, of course, been much discussion about harmonizing the law of contract in the member states of the European Union. The existence of separate, national, laws of contract can be seen to impede the development of internal market. Nevertheless, the current most significant move, on that front, seems to be towards the adoption of a Common European Sales Law, merely as an option, which parties could choose to use in contracting. The common law seems to be alive, and well, and continuing to evolve, at least for the time being.

Further reading

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