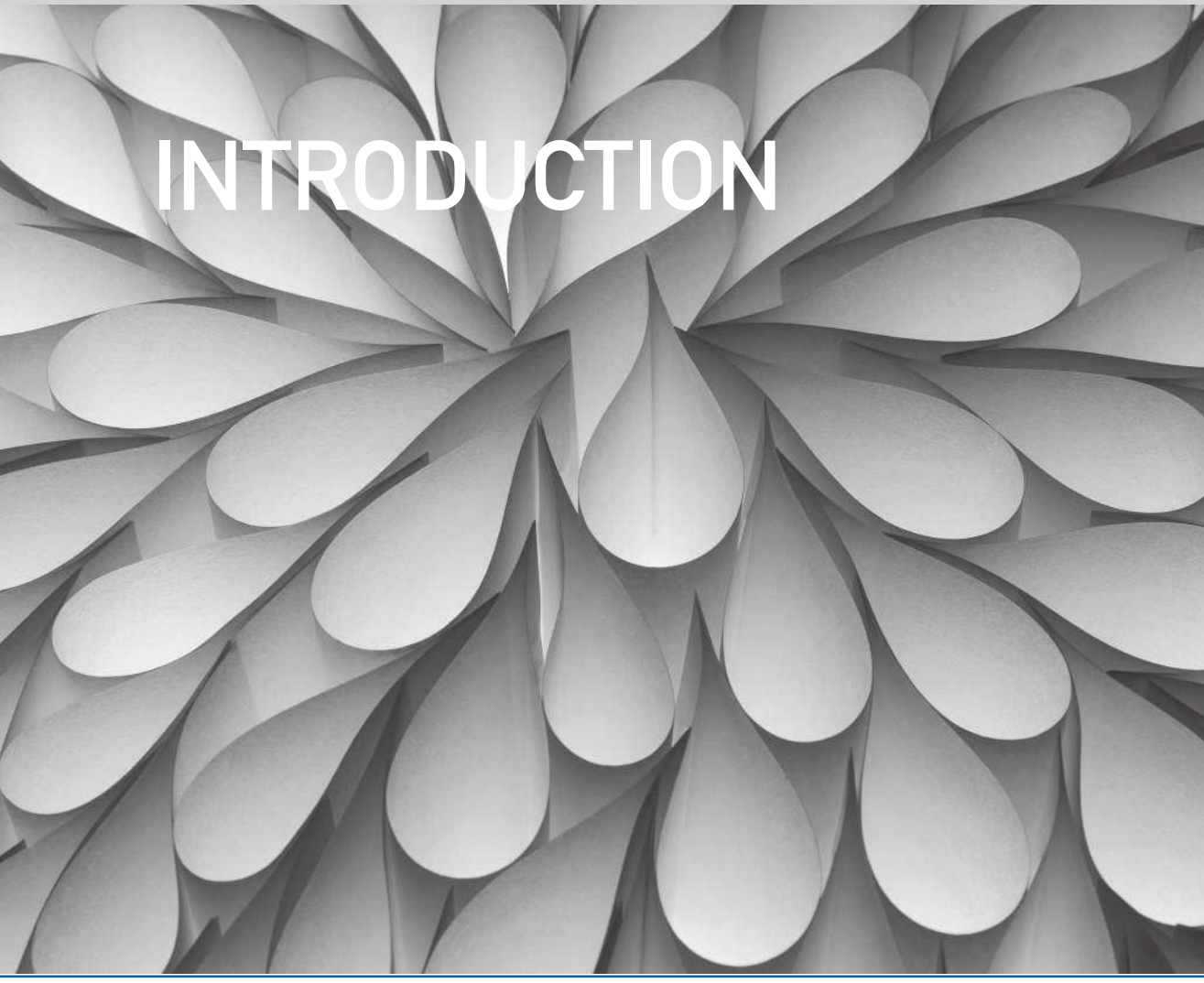
PART

INTRODUCTION



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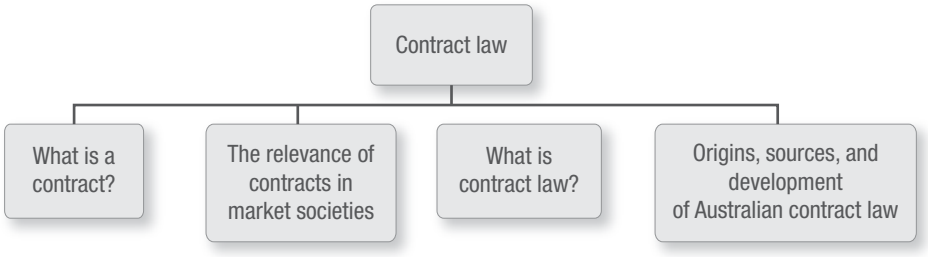
SOME BASIC QUESTIONS

1.1 Overview

This chapter deals with some basic questions which surround the contract law dimension. The concepts of 'contract' and 'contract law' are introduced. It will discuss why the law distinguishes between contracts and transactions that are not legally binding, and thus, unenforceable. In so doing, it will show why the notion of 'bargain' lies at the core of contractual arrangements. Furthermore, it will show why contracts underpin market societies and why the concept of contract is being increasingly fragmentised. Finally, attention is paid to the English origins of Australian contract law, as well as to its modern and contemporary sources.



1.2 What is a contract?

Factor	Short explanation	Relevant authorities	*Principles* text*
Contract as promise	A contract is a legally enforceable promise	JW Carter, E Peden and GJ Tolhurst, *Contract Law in Australia* (LexisNexis Butterworths, 5th ed, 2007) B Coote, 'The Essence of Contract – Part I' (1988) 1(1) *Journal of Contract Law* 91 JW Carter, *Australian Contract Law* (Butterworths LexisNexis, 6th ed, 2013)	Chapter 1: 1.02

* Consult the corresponding section(s) of the *Principles* text for more detail.

Contracts are a class of obligations.[1] In Australia, a contract is an agreement between two or more parties, involving one or more promises that are given for something in return, and that the parties intend to be legally enforceable. The term 'party' refers to an individual or an artificial entity (such as a corporation or a state) that the law treats as if it were a person.

1 Andrew Burrows, *Understanding the Law of Obligations: Essays on Contract, Tort and Restitution*, (Hart Publishing, 1998); Keith Mason, John W Carter and Greg J Tolhurst, *Mason & Carter's Restitution Law in Australia* (Butterworths LexisNexis, 3rd ed, 2016).

Corporations or governments can enter into legally binding agreements, even though they necessarily have to act through the agency of human beings: see **4.1**, **8.2**.

Contracts are voluntary undertakings: *Australian Woollen Mills v Commonwealth* (1954) 92 CLR 424, 457. The parties are left free to decide whether or not to negotiate and/or bind themselves to each other: see **5.2** and **6.3**. From this, it follows that it is illegal to coerce a party into a contract by threats or undue pressure: see **19.2**. Yet, both freedom of contract and equality of bargaining power are 'assumptions'[2], which, in real-life situations, have to be adjusted. Further, in certain cases, such as when dealings are made with standard-form contracts or when one party is a consumer, these assumptions are reverted: see **4.4**, **9.2, 11.2**, **20.3**.

Australian contract law is informed by the view which understands contracts as bargains: the law compels the person who made the promise ('the promisor') to perform the promise or pay damages for non-performance only if something is given or promised in return by the other person ('the promisee'[3]). Hence, a promise is legally binding only if it is made under seal or supported by 'consideration': see **5.6**. The latter is a technical term which refers to that which is given or accepted in return for a promise ('*quid pro quo*'). Scholars tend to argue that the view that understands contracts as the law of bargains emerged in the nineteenth century to counter-balance the erosion of the classical will theory as brought about by the adoption of an objective model of contracting. Consideration, it is further maintained, is the product of this view. Yet it has been noted that the will theory was the dominant model of contract until the twentieth century, and the idea that contracts are based on exchange long predates the nineteenth century in the doctrine of consideration.[4] What matters for our purposes, however, is that the bargain theory established itself also against the promise, reasonable expectations, and reliance theories: see **2.3**.

Further requirements for an agreement to be legally binding are the parties' intention to create legal relations (a requirement which is directly related to the principle of free consent, mentioned above) and their capacity to bind themselves in a contractual relationship. Importantly, in some cases, the law also prescribes that the terms of a transaction are set out in a formal document. Hence, certain contracts may be required to be in writing or by deed, as well as evidenced in writing: see **5.9**. As only the promises that meet these requirements are contracts, it is of the essence to distinguish between contractual relationships and arrangements which the law does not categorise as such, and thus, cannot be enforced because they are not legally binding. The doctrine of estoppel plays a fundamental role in this respect as it allows a promisee to go to court and hold a promisor to their commitment, where the promisee has relied on the promise to their detriment: see **7.2**.

2 John W Carter, *Contract Law in Australia* (Butterworths LexisNexis, 6th ed, 2013) 8, extract below.

3 See John W Carter, Elisabeth Peden and Greg J Tolhurst, *Contract Law in Australia* (Butterworths LexisNexis, 5th ed, 2007) at 1-01, extract below.

4 David Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford University Press, 1999); Nick Seddon, Rick Bigwood and Manfred Ellinghaus *Chesire & Fifoot Law of Contract* (Butterworths LexisNexis, 10th Australian ed, 2012) 1263; Warren Swain, *The Law of Contract 1670–1870* (Cambridge University Press, 2015).

JW Carter, E Peden and GJ Tolhurst, *Contract Law in Australia* (LexisNexis Butterworths, 5th ed, 2007)

[1-01] A contract is a legally binding promise or agreement. The person (or persons) who makes a promise is termed the 'promisor'. The person (or persons) to whom the promise is made is termed the 'promisee'.

B Coote, 'The Essence of Contract – Part I' (1988) 1(1) *Journal of Contract Law* 91

[94] Almost invariably, common law textbooks have defined contracts in terms of promise or agreement or of a combination of the two. And, as we shall see, promise and agreement are linked respectively to what have been, historically, the two main contract theories.

A third element in some definitions has been a statement that contracts create rights *in personam* rather than rights *in rem*; that being [95] a distinction which descends from Roman law. For present purposes, its significance is twofold. It requires of a contract that, at its formation, at least some element should still need to be performed or fulfilled. It therefore excludes from the category of contracts transactions, such as conveyances, which have the effect of granting or transferring rights *in rem* by the very fact of being executed.

1 In terms of agreement

Of the leading modern English contract texts, both *Treitel* and *Cheshire and Fifoot* define contract in terms of agreement. Definitions in those terms go back to *Doctor and Student* in the sixteenth century and to such later works as *Blackstone* and the earlier editions of *Chitty.* The current edition of *Treitel* states that a contract is 'an agreement giving rise to obligations which are enforced or recognised by law'. Such definitions have the advantage of being centred on an incident of the vast majority of contracts whether under common law or under the systems which derive from Roman law. In that sense, they correspond with popular perceptions of what contracts are about. Their disadvantage is that if they are confined to agreements they necessarily exclude contracts which are not agreements. Such contracts can be made at common law by the use of a deed and they have their equivalents under the Scottish system, for example. For this reason, if no other, a number of writers who include agreements in their definitions refer also to promises in the alternative.

An alternative response would be to deny that arrangements made without agreement can be contracts at all. This is what *Cheshire and Fifoot* have done.

> [A party] is [by deed] bound, not because he has made a contract but because he has chosen to act within the limits of a prescribed formula. The idea of [96] bargain, fundamental to the English conception of contract is absent. An Englishman is liable, not because he has made a promise but because he has made a bargain.

By combining agreement with the notion of bargain in their definition of contract under English law, the learned authors have raised a second set of problems, to which reference will be made when the bargain theory comes to be considered.

2 In terms of promise

Of all English textbook definitions of contract, the most famous is probably that by Sir Frederick Pollock. A contract, he wrote, is 'a promise or set of promises which the law will enforce'. The definition contained in the American *Restatement of the Law of Contracts* is not dissimilar:

> A contract is a promise or set of promises for the breach of which the law gives a remedy or the performance of which the law in some way recognises as a duty.

Definitions in such terms have the advantage of being wide enough to cover contracts which are not the subject of agreements. Their disadvantage is that they may be too comprehensive. They are wide enough to include promises which the law enforces even though neither deed nor consideration is present. Amongst them would be those promises enforceable under the law of torts or by reason of estoppel which have, in recent times, raised questions about the limits of contract.

They are promises of a kind which led to the inclusion of s 90 in the *Restatement of the Law of Contracts*, and they may frequently form part of courses on the law of contract. But whether they should now be classed as being themselves contracts is, in effect, what the present inquiry is about. In classical common law contract theory, at least, it is clear that in the absence of either seal or consideration they could not be so considered.

Another supposed disadvantage of definitions in terms of promise has sometimes been thought to lie in the very nature of a promise. Some philosophers and others have assumed that promises must involve the [97] doing (or refraining from doing) of some act in the future. If promises were so limited, there could, prima facie, be no place in contract for a warranty, the essence of which is a statement of past or present fact rather than the promise of something to be done in the future. On this sort of reasoning, s 2(2) of the Restatement of Contracts provided that warranties were to be treated as promises or undertakings to be answerable for damage caused by the non-happening of the event or the non-existence of the fact warranted. The effect of that provision was to substitute the secondary for the primary obligation. The better view is that past or present fact can be the subject of a promise. To suppose otherwise, it will be suggested, is to misunderstand the distinguishing characteristic of a promise.

JW Carter, *Australian Contract Law* (Butterworths LexisNexis, 6th ed, 2013)

[8] [1-08] **Paradigm situation**. The modern law of contract assumes freedom of contract; that is, freedom to decide whether to contract and to negotiate contractual terms. It also assumes a paradigm situation of one-to-one negotiation of all the terms of an agreement by parties with equal bargaining strengths concerned to maximise their individual positions. It must be recognised that although it is without doubt 'an attribute of a free society … that it is generally left to the parties themselves to make bargains' [quoting *Biotechnology Australia Pty Ltd v Pace* (1988) 15 NSWLR 130, 133 K(irby P)] these assumptions are frequently contradicted or qualified by events in the real world. In many situations adjustments must be made in the conception or application of principle based on these assumptions.

QUESTIONS

(1) What is a contract?

(2) In what terms can a contract be defined?

(3) Why do the notions of 'binding promise' and 'bargain' lie at the core of contractual arrangements?

1.3 The relevance of contracts in market societies

Factor	Short explanation	Relevant authorities	*Principles* text*
Contracts underpin modern economies	Market exchanges lie at the root of modern society Contract is the tool through which most exchanges are made	H Collins, *Regulating Contracts* (Oxford University Press, 1999) P Zumbansen, 'The Law of Society: Governance Through Contract' (2007) 14(2) *Indiana Journal of Global Legal Studies* 191 S Mouzas and M Furmston, 'A Proposed Taxonomy of Contracts' (2013) 30(1) *Journal of Contract Law* 1	Chapter 1: 1.01 Chapter 2: 2.04

* Consult the corresponding section(s) of the *Principles* text for more detail.

Humans' progression from ancient forms of aggregation to the modern form of polity would not have been possible without the intensification of trade and the evolution of exchange methods. In a classic work on the subject, which was written under the influence of the modern process of industrialisation, Sir Henry Maine contended that such progression reflected that from 'status to contract'.[5] This is certainly correct: market exchanges lie at the root of modern society and contract is the tool through which most exchanges are made.

Notwithstanding the above, it should be borne in mind that contracts' function depends on our conceptualisation of them, which in turn depends on which theory is used to operationalise them. By way of an example, the will theory and the bargain theory are two different expressions of an individualistic understanding of contractual relationships: the former gives priority to the parties' *subjective* intention, whereas the latter—upon which, as mentioned, Australian contract law is based—to their agreement as *objectively* expressed through the 'reciprocal conventional inducement' (see **2.3**)[6].

5 Henry Maine, *Ancient Law. Its Connection with the Early History of Society and Its Relations to Modern Ideas* (John Murry, 14th ed, 1981) ch 5.

6 Brian Coote, 'The Essence of Contract – Part I' (1988) 1(1) *Journal of Contract Law* 91–112, 101.

In short, it may be said that the notion of contract is a socio-legal one. The reason for this is two-fold: first, as a form of 'association', contracts are the 'law of society'[7]; second, the role that contractual agreements play in societal development depends on our conceptualisation of human relations as well as on the function that we assign to (contract) law in regulating them. Proof of this is given by what contracts are currently undergoing: the sophistication of trade and pluralisation of regulative phenomena at the global, transnational, and local levels has led to the need to develop new taxonomies which decode the functioning and effect of contracting in its various aspects.[8] For the very same reason, there is the tendency to divide between 'governance *by* contract' and 'governance *of* contract'.[9]

H Collins, *Regulating Contracts* (Oxford University Press, 1999)

[13] Before examining any regulation of contracts, we should devote some time to the idea of a contractual relation itself. This relation plainly differs from other types of human association, such as those found between friends, neighbours, members of a club, and between members of a family. Such an investigation of the social institution of contract presents a considerable problem, because the idea of contract possesses a confusing surplus of meanings.

We use the idea of contract in numerous contexts: from a commonplace purchase of goods from a shop, to abstract theories of the foundations of political obligations in modern societies, the Social Contract. Furthermore, each conception or use of the idea of contract can be examined from a variety of perspectives or discourses, including morality, politics, economics, and law. We can ask of both the shop purchase and the hypothetical Social Contract; is the bargain fair, just, efficient, or binding?

Even within a particular discourse such as law, we discover a rich variety of themes and emphases about contracts. The practising lawyer identifies the key function of contracts as the planning of an economic relation. The legal scholar views the rules of contract law as a particular source of private law obligations. The socio-legal scholar perhaps considers contract law as a tool for the regulation of economic and social transactions. Finally, the judge treats contracts as creating binding rules of law between the parties, breach of which provides a justification for the imposition of state sanctions.

This multiplicity of contexts and meanings signifies that the idea of contract is used not only to describe a key economic institution in a market economy, but also to express more generally a central form, of human association in modern society. [. . .]

How Contract Thinks About Association

A contract creates a relationship between people. It comprises a distinctive type of human association. What distinguishes a contractual relation from [14] other forms of association, such as links of status, kinship, friendship, and membership of a community or an organisation? Some caution is required in answering this question, because contract is such an abstract idea that many kinds of relationship such as marriage or an exchange of gifts between friends can be perceived, at the price

7 Hugh Collins, *Regulating Contracts* (Oxford University Press, 1999); Peer Zumbansen, 'The Law of Society: Governance Through Contract' (2007) 14(2) *Indiana Journal of Global Legal Studies* 191–233, extracts below.

8 Stefanos Mouzas and Michael Furmston, 'A Proposed Taxonomy of Contracts' (2013) 30(1) *Journal of Contract Law* 1–11, extract below.

9 Zumbansen (n 7), extract below.

of some distortion, as contractual. My contention is, however, that a paradigm meaning can be attributed to the idea of contract.

[. . .]

When we try to distance ourselves from the legal conception of the meaning of contractual relations, we can observe that contracts establish [15] a discrete communication system between the individuals. Whatever their prior relationship, a contractual agreement constitutes a distinct and isolated specification of particular undertakings. The contract may be made between friends, for example, who already have diffuse expectations of loyalty and support established through previous interactions including exchanges. [. . .] The contractual relation creates new, more specific expectations, but simultaneously it tends to exclude the surrounding normative context in the evaluation of whether those expectations have been fulfilled or disappointed.

Furthermore, unlike other social interactions which may create diffuse expectations for the future, such as the formation of a friendship or the making of a gift, a contractual relation empowers the parties to create their own distinct understanding of how this particular relationship should proceed.

[. . .]

The contract constructs an image of the human association that reduces its complexity to the elements and trajectories that have significance within the contractual framework. The contract thinks about events, for instance, by examining human actions and words within a narrow timeframe; the prior pattern of the social [16] relation between the parties and their sentiments of trust and loyalty are irrelevant to this construction of knowledge.

[. . .] Four characteristics of the meaning of contractual association stand out in this approach.

(1) The association marked by a contract consists of isolated or discrete commitments, which have an exclusionary force in practical reasoning, so that these commitments tend to displace other normative standards derived from the social context of the contractual relation, including other forms of association such as friendship and status. Contract therefore reduces the complexity of human association, rendering social relations susceptible to management and reconstruction.
(2) The commitments identified by a contract tend to be temporary and specific. Contract therefore reasons about associations in such a way that they can either be completed (the money is exchanged for the goods) or broken (no payment is made). Association is therefore understood by contract as finite in duration, and always susceptible to dissolution.
(3) Contract thinks about association as a personal bond between the parties to the agreement, so that it neither imposes obligations on others nor confers any rights on third parties. This personal bond is a private relationship between individuals rather than a social undertaking towards a community.
(4) Contract thinks about association as an artificial and almost infinitely malleable construction, the product of a voluntary choice by individuals.

The way in which the contract thinks about the relation is not the same as the way in which the law of contract thinks about the same events. Both [17] communication systems construct their own knowledge of the world within their own criteria of relevance. It is quite possible, for instance, for two people to believe that they have entered a contractual relation, and permit that framework to provide a normative guide to their behaviour, even though in law the events do not count as a contract at all. The differences between the two communication systems will be of great interest to us here, but for the time being we concentrate upon the contractual relation rather than legal reasoning.